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FOREIGN ASSISTANCE AND RELATED PROGRAMS APPROPRIATIONS FOR FISCAL YEAR 1988

HEARINGS

BEFORE A

SUBCOMMITTEE OF THE COMMITTEE ON APPROPRIATIONS UNITED STATES SENATE

ONE HUNDREDTH CONGRESS

FIRST SESSION

ON

H.R. 3186

AN ACT MAKING APPROPRIATIONS FOR FOREIGN ASSISTANCE AND RELATED PROGRAMS APPROPRIATIONS FOR THE FISCAL YEAR ENDING SEPTEMBER 30, 1988, AND FOR OTHER PURPOSES

PART 4 (Pages 1-69)

TITLE IV—EXPORT FINANCING PROGRAMS
TRADE CREDIT INSURANCE PROGRAM
TRADE AND DEVELOPMENT
EXPORT-IMPORT BANK OF THE UNITED STATES
OVERSEAS PRIVATE INVESTMENT CORPORATION

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FOREIGN ASSISTANCE AND RELATED PROGRAMS APPROPRIATIONS FOR FISCAL YEAR 1988

TUESDAY, JULY 28, 1987

U.S. SENATE,
SUBCOMMITTEE OF THE COMMITTEE ON APPROPRIATIONS,
Washington, DC.

The subcommittee met at 9:02 a.m., in room S–126, the Capitol, Hon. Robert W. Kasten, presiding.

Present: Senators Mikulski, Kasten, and D'Amato.

EXPORT-IMPORT BANK

STATEMENT OF JOHN A. BOHN, JR., PRESIDENT AND CHAIRMAN, EXPORT-IMPORT BANK

OPENING STATEMENT OF SENATOR KASTEN

Senator KASTEN. This morning, we will be receiving testimony concerning four programs combining our Nation's commitments to both trade and also to development. Second, each works closely with the private sector to achieve these objectives.

The private sector is always playing and will continue to play a vital role in our development programs. On one level, U.S. businesses are properly concerned that they receive a fair opportunity to participate in development projects. On another level, we all realize that our economy is intertwined with the world economy. As a major exporter, our own economic future depends on the growth of markets worldwide.

We look forward to the testimony this morning, and to working with John and the Eximbank as we develop our Foreign Operations Appropriations Bill for 1988.

The first witness this morning is Mr. John Bohn, the President and the Chairman of the Eximbank, but first I would like to ask whether Senator D'Amato or Senator Mikulski or others, have any opening statements.

PREPARED STATEMENT OF SENATOR D'AMATO

Senator D'AMATO. Mr. Chairman, I am going to ask that you give me permission to put my statement into the record as if read in its entirety, but I would be remiss if I didn't point out the valuable contribution that the Eximbank has made not only to the nation in terms of helping us as it relates to exports and to foreign countries where we come un-

der increasingly difficult times in making the traditional foreign assistance available, but to New York in particular. Exim has been invaluable to New York exports. From 1982 to 1985, New York businesses exported nearly $5 billion in goods with Eximbank assistance.

We certainly are mindful of its importance to our national and to my own state's economic prosperity, not to mention the least of which the opportunity that it provides for the private sector development and use in third world nations and in Central America without which, I think, we would have great, great problems and tremendous social unrest.

I am going to ask that the balance of my statement be included in the record.

Senator KASTEN. Without objection, your entire statement will be included in the record.

[The statement follows:]

PREPARED STATEMENT OF HON. ALFONSE D'AMATO

U.S. SENATOR FROM NEW YORK

Mr. Chairman, I welcome John Bohn, the President and Chairman of the Export-Import Bank, Irwin A. Leavy, from the Bureau for Latin America, Christian Holmes, Director of the AID Trade and Development Program, and Craig Nalen, President and CEO of the Overseas Private Investment Corporation.

The Senate recently has been preoccupied by the issue of fair trade. The programs reviewed today are positive influences on our trade balance. Unfortunately, they only help prevent the bleak trade picture from becoming even worse.

The Exim Bank, OPIC, AID's Trade Credit Insurance Program and Trade and Development Program all assist U.S. businesses to sell their goods and services abroad. Since its creation in 1934 the EXIM Bank has facilitated more than $180 billion in U.S. exports. Through various loan, guarantee, and insurance programs, the EXIM Bank has provided American exporters with financing that is competitive in the world market, reducing the risks associated with the export business. I would be remiss if I did not note that the EXIM Bank has been invaluable to New York exporters. From 1982 to 1985, New York businesses exported nearly $5 billion in goods with EXIM Bank assistance.

On a smaller scale, the U.S. Trade and Development Program fosters improved U.S. trade by financing the planning of projects abroad, predominately in nations which receive U.S. foreign assistance. In light of recent Congressional criticism of our foreign aid program, I believe this approach should be expanded. At least it seeks some return on our aid program investment.

The Trade Credit Insurance Program provides guarantees for financing transactions involving U.S. exports for private sector use in Central America. TCIP, which grew out of the Kissinger Commission report on Central America, funds imports from the United States primarily for Central American export industries.

OPIC encourages U.S. private investment in developing countries. While the link with U.S. trade is not direct, there is a definite trade benefit, since U.S. investors can usually be relied on to use a significant amount of U.S. goods or services on an overseas investment.

We must continue to support those programs that assist our businesses to compete abroad. These programs cannot match our competitors' subsidies and other forms of unfair trading practices. They can, however, continue to provide a healthy boost for our trade balance while keeping our businesses active in the world marketplace.

Thank you, Mr. Chairman.

INTRODUCTION OF JOHN BOHN

Senator KASTEN. Senator Mikulski, do you have an opening statement, or should we begin with the testimony?

Senator MIKULSKI. This is certainly a very interesting bipartisan meeting. It certainly seems like the old days, doesn't it, Bob?

Senator KASTEN. Yes. This is a bipartisan committee.

Senator MIKULSKI. Actually, it is, and I think that we ought to just get down to hearing our witnesses.

Senator KASTEN. John, we look forward to your testimony.

Mr. BOHN. Thank you very much, Mr. Chairman. It is a pleasure, as always, to be here.

What I would like to do is spend just a few minutes this morning, breaking up my comments into two parts, reviewing briefly what the market looks like to us, our response in terms of our new programs, and then some observations about where I think we are going and how I think we need to get there.

CURRENT MARKET CONDITIONS

The one thing that was clear by the end of 1986, certainly, was that the marketplace had changed a great deal from the old days of Eximbank. What we were seeing were smaller projects, products and services exports as distinguished from the large megabuck projects which had been the traditional activity of the Export-Import Bank. Partly because of the debt crisis, partly because of other adjustment factors going on in the developing world, that kind of demand had largely subsided.

Secondly, we saw, again partly as a result of the debt crisis, and lending by banks in the past, that most, not all, but most of the commercial banks had developed a significant aversion to taking foreign risk. The result of that in the trade area was that many companies which had traditionally gone to commercial banks for trade support simply were no longer able to do so. In the competitive world, when foreign banks and foreign suppliers were becoming more active in a decreasing market, the lack of bank support was a significant negative factor as far as American exporters were concerned.

As a result of those two observations and extensive studies with a number of bankers and a number of the members of the exporting community, on May 1 we launched a series of new programs, the principal purpose of which was to address the needs of the medium term exporter—the medium size company that had use for medium term credit. All of our program changes on May 1 were designed to do that, and I think so far we are making some significant progress in getting those finalized and getting them out into the marketplace.

Clearly what is still a problem is government subsidized exports on a broader scale, and I will come back to that in just a minute.

We had to simplify and streamline our programs, and, as a result of last year's legislation and our own studies, try to involve more of the capital markets, more private participation, in the funding exercise. All of that we began on May 1, and my sense is that we are making progress.

Key to that, Mr. Chairman, is our ability to stay open on a more predictable basis, to be able to make judgments which will permit exporters to plan in advance. I think the most important part of that probably is to go to a country-differentiated fee structure, which we think over time will permit us not only to stay open longer in more countries, but, more importantly, permit us at the same time to break even.

MIXED CREDITS NEGOTIATIONS

Anyway, so much for where the market is going. One comment on the OECD discussions, which are always very much of interest to this committee and others in terms of where we go in the mixed credit area. We have made a substantial breakthrough, I think, Mr. Chairman, in the sense that beginning July 1 of this year, the grant element required has gone up to 30 percent. Moreover, in July of 1988, it will go up to 35 percent, which will make, I think, a much clearer distinction between aid or mixed credits and the classic export credit kind of transaction.

I would be remiss if I thought it would solve the problem. I think that we are still in for considerable competition from concessionary loans and concessionary credits given by aid-related agencies in the international marketplace, but I think, with this distinction, increasing the cost of this kind of financing will reduce, at least to some extent, the incidence of the mixed credit problems that we have had in the past.

DIRECT CREDIT AND GUARANTEE AUTHORITY USAGE

One of the issues that I would like to spend just a few minutes on is this issue of usage. Each year, we come before the committee having requested a certain level of direct lending and guarantee authority. Each year, since I have been here, we have substantially under-performed what we have requested, and I think that it is important that we deal with that issue directly.

As of June 30, 1987, we have used about $344 million of our direct lending authority. We have used about $6.3 billion of guarantee authority for total authorizations of about $6.6 billion. It is important to understand, Mr. Chairman, that the interest rate adjustments in the marketplace have a very profound effect on whether a given borrower goes to our guarantee program, particularly our financial guarantee program, or our direct lending program. So when you see a decline, as you do in direct lending, when we under-perform on the direct lending program, one has to look at the financial guarantee program, because when the market rates are lower, most of the users will go to the financial guarantee program. It is certainly cheaper for them.

Through 1986, there was about a 75 basis point difference on the average in favor of using the financial guarantees. I don't have the figures for the first half of 1987, but my guess is that, until the last month or two, that discrepancy probably continued.

Senator D'AMATO. Could I ask you something for just a moment?

Mr. BOHN. Sure.

Senator D'AMATO. I was mentioning to the chairman. Does that give you greater leverage, the financial guarantee, as opposed to the direct loan?

Mr. BOHN. When you say "leverage," I am unclear.

Senator D'AMATO. Let me ask you. For example, as it relates to a financial guarantee, do you have a larger number of loans as it relates to a financial guarantee as opposed to the direct loan?

Mr. BOHN. It is really a function of what is cheaper for the borrower. We have financial guarantee transactions that go up into $200 or $300 million just as we have direct lending that will go up to that size. What happens is that a borrower will come in and we will typically give an either/or commitment. At the time of authorization, the borrower and his financial manager will decide whether it is cheaper for them to borrow with our guarantee or take the direct loans that we provide.

Senator D'AMATO. I understand that. Actually, my point was, is there any difference in the capacity which you have, for example, do you get greater leverage as a result of making a guarantee as opposed to a direct loan?

Mr. BOHN. We have a greater capacity in the appropriations process when we utilize guarantees. The reason for that is simply a scoring reason.

RESERVES

Senator D'AMATO. Do you put a certain amount in reserve?

Mr. BOHN. Yes, we do.

Senator D'AMATO. What amount do you put in reserve as it relates to guarantee?

Mr. BOHN. Twenty-five percent.

Senator D'AMATO. So your leveraging factor, you can make much more in the way of loan guaranteeing as opposed to a direct loan. Is that correct?

Mr. BOHN. Yes.

Senator D'AMATO. I simply wanted to ascertain whether or not that was the case.

Mr. BOHN. In the market process, Senator, what happens is that the use of loans or guarantees is almost strictly a function of cost. So we don't always have the option of choosing one or the other. It is a function of the competitive position of our supplier with respect to the competition.

Senator D'AMATO. It seems to me that it behooves both sides, if you can do the guarantee, you get greater leverage. I am going to back off, but I just wanted to go through that process, then obviously the market conditions giving that loan at a cheaper rate.

Mr. BOHN. There is another part of that, if I might offer it, and that is, in about 1983 we were able to negotiate a change in the OECD agreement on officially supported interest rates which provided for a tie between a basket of currencies in Europe and the OECD consensus rate.

In the early 1970s, no such tie existed so there were huge 500 and 600 basis points subsidies in our loans, which is the reason for the losses that we suffer now. We were lending money at 7 and 8 percent, and borrowing those same funds at 12, 13, and 14 percent. That is probably no longer possible over a protracted period of time because in the interim we have negotiated this tie between the basket of currencies and the OECD consensus rates. The interest rate, which is based on that basket of currencies, is adjusted every 6 months, so you don't have this protracted period when you can be way under water as you could in the 1970s.

Just looking at activity, which I think is important, apropos of what you said, our financial guarantees, for example, are 136 percent over what they were fiscal-year-to-date in 1986. Our medium term credits are about 27 percent over. Short term insurance is 50 to 60 percent over. Our total guarantees and insurance are about the same. Our authorizations are up about 40 percent, and the export value supported by the Bank is up about 65 to 70 percent over what it was in 1986.

So we are beginning to see more activity partly as a result of the new programs and partly as a result of the adjustment in the dollar, which is giving our exporters a much better handle on what is going on.

Incidentally, we are the largest net contributor on the positive side to the Budget Function 150. In 1987, we will contribute on the positive side, that is, excess of inflows over outflows, almost $2.4 billion. In 1988, the estimate is about $1.6 billion. So in this particular period, we are a positive contributor to Budget Function 150, and this just happens to be a result of financial flows and increase of repayments over disbursements.

FY 1988 REQUEST

When we look at 1988, which is what we are here to look at, we go through the problem each year of trying to estimate what our demand is going to be, particularly in the direct lending area. We estimate that for this year, for example, and we have just gone through this process again about 2 weeks ago, demand for direct lending in 1987 will be about $900 million.

As you know, with the rescission bringing us down to $680 million, our best estimate at this point is a need for carryover of about $320 million. We then go through utilization of this econometric model, looking at such things as inflation rates, global growth rates, and positing no particular crisis that is going to disrupt the system as far as debt is concerned, for fiscal year 1988.

We estimate that in the long term area, we are talking about $810 or $820 million. We add to that $150 million in the medium term, based on our new accounting procedure which is more conservative than it was before. So we add that together and we get about $1.2 billion, or whatever that comes out to be, $1.270 billion, in terms of our best judgment of what our demand will be in 1988.

Again, whether our direct loans will reach that will be largely a function of the interest rate structure, and how that comes together. I think,

again, if we are going to get into a period when the interest rates will go up, direct lending is apt to be used more than others.

Two comments, if I might, one on the war chest. There have been some comments that the war chest is no longer necessary, because of having reached at least tentative agreement with the OECD. My experience in this exercise would lead me to believe that there is going to be great pressure to grandfather, that is, great pressure to try to keep some of these old deals in at the lower rate. I would urgently suggest that the war chest is certainly important for us to police this interim process. It is one of those things where I can almost guarantee that there will be a need to do that over this next year.

With respect to the administrative expense budget, I just want to touch on that. You will recall that as a result of last year's legislation, we have now direct access in those situations where the exporter doesn't want to go to a bank, they want to come to Eximbank directly. That has increased the volume and the new programs have increased the volume substantially, particularly given our almost complete initiative process as we devote ourselves toward the medium size and small business.

INFORMATION SERVICES

The other major item, in addition to personnel, in the administrative budget is information services. We simply have to automate. We simply have to be able to speed up and streamline our processing, and provide the necessary management control.

It is simply a more complex world, and to manage the assets of the Bank intelligently and provide the kind of service that is responsive to the real world, we simply need to make these investments in management information services.

Mr. Chairman, that is really all I have as an introductory statement. I will be happy to answer any questions that you may have.

[The prepared statement follows:]

PREPARED STATEMENT OF JOHN A. BOHN, JR.

PRESIDENT AND CHAIRMAN

EXPORT-IMPORT BANK OF THE UNITED STATES

Mr. Chairman and Members of the Subcommittee:

It is a pleasure for me to appear before you today to present Eximbank's budget request for fiscal year 1988. Our request will enable us to operate the new programs that went into effect on May 1. Before discussing numbers, I would like to spend a few minutes on the programs themselves which are the result of the most thorough review of the Bank's activities since 1960.

In carrying out this review, we kept in mind that our statutory mandate is to help American exporters by meeting government-supported competition from other countries and correcting market imperfections. We were guided by the realities of the market, the needs of American exporters and American taxpayers, government-wide budgetary concerns and the prudent use of government credit.

The changes in international economic realities over the past decade have had a tremendous impact upon Eximbank's activities. In the 1970's, Eximbank helped U.S. exporters build large projects in dozens of countries, assisted in developing the infrastructure in Brazil and Mexico, made loans to develop natural resources in Asia, and expanded manufacturing throughout the world. We provided funds for power development and financed the export of a lot of airplanes.

By the 1980's, everything had changed -- the nature of the exports, the markets, the type of financing needed. We still see some large projects, but small projects, shelf items or individual pieces of equipment and services are accounting for a larger and larger share of our business.

We also found that commercial banks have largely withdrawn from financing exports, shutting out American exporters from already shrinking developing country markets. Deregulation and increasing competition have focused attention on bottom line results, and high overhead export finance has been less profitable than other banking services. Trade finance departments have been eliminated or drastically cut back because commercial banks have little appetite for country risk.

To summarize, exporters now need financing in riskier markets and on deals which are smaller and which take longer to put together and close. Lenders, however, want less risk, greater profit margins, and activities which are transaction-oriented and less labor-intensive.

At the same time, U.S. exporters are still facing competition from foreign government-subsidized exporters in pursuit of systematic schemes of market domination. Subsidized financing is a continuing problem in certain

industries and in certain markets. Tied aid credits are the prime example of continuing pernicious practices.

In analyzing the needs of our exporters, it became clear to us that Eximbank had to assume a broader range of explicitly defined country and transaction risks than it had previously. Programs and procedures needed to be simplified, streamlined and internally consistent. They had to be accessible to the widest variety of potential sources of export finance, including capital market participants. Guided by these principles, we concluded that our new programs had to contain the following elements:

-- Eximbank would focus on the needs of the middle market product or service exporter.

-- Eximbank would have essentially one loan program and one guarantee program for both medium-term and long-term export transactions.

-- Both programs would operate through preliminary commitments and would be open to any responsible party.

-- Both programs would provide up to 85% financing, the maximum permitted under the OECD consensus. Eximbank loans would carry the minimum interest rate allowed by the OECD rate schedule for the market and the term.

-- Eximbank would absorb country risk in a way that is clear and consistent.

-- Eximbank's fees would be comparable for both programs, based on a country/buyer/term differentiated structure and would be competitive with those charged by other export credit agencies.

-- Eximbank's guarantee would be upgraded and would establish up front exactly how much interest and principal would be covered to eliminate past uncertainties.

Beyond these program changes, I want to emphasize that Eximbank has taken other steps to promote the President's trade policy of keeping international markets open on a freely competitive basis. As I said before, we assist American companies in countering foreign-subsidized competition. In addition, over the past three years, the U.S. Government -- in particular, Eximbank and the Department of the Treasury -- have been negotiating with our OECD counterparts to raise the level of the minimum grant element in tied-aid credits. At the President's direction, Eximbank has continued an aggressive campaign of targeted mixed credit action directed against countries which have been impeding these negotiations.

Partially in response to our efforts, the OECD has proposed to tighten the rules governing the use of tied aid and other subsidized concessionary loans which distort international trade. I am pleased to say that the proposals have been accepted. The rule changes are being implemented in two stages -- the first took place on July 1, 1987 and the second will occur in a year.

Two important changes are causing OECD countries,

particularly those with low rates of interest, to find the costs of mixed credits and other forms of tied and partially tied aid financing much more expensive when the proposed rules take full effect. First, mixed credits and other forms of tied aid will only be permitted if the financing offer contains an outright grant or a soft loan so concessionary that it is equivalent to a grant of at least 35 percent of the value of the transaction. For a small group of the poorest developing countries, known as the Least Developed countries, this minimum "grant element" will be 50 percent. Second and more important for low interest currency countries, the rules for equating soft loans to grants will be changed so that interest rates in the financial markets of each currency will become the dominant factor in the calculation instead of the present uniform factor of 10 percent.

This proposal represents an important step at a crucial time, and it has been accepted by the major exporting countries of the world including the European Community, Canada and Japan as well as the United States. The new rules will force a clear distinction between trade finance and truly concessionary development aid. After the changes are fully implemented in July 1988, countries wishing to offer development aid will be more likely to provide grants or truly concessionary loans in the poorest areas and for true aid purposes. It will be much more costly to distort competition in export credit transactions by mixing in small amounts of grant money or by making loans which slightly undercut the guidelines for official export credits but which do not represent any significant cost to the lending government. I expect the new guidelines to reduce the frequency of mixed credits in competitive transactions without reducing the flow of truly concessionary loans and grants for projects in countries which require such financing.

As part of our efforts to encourage negotiations on tied aid credits, earlier this fiscal year we extended two lines of credit of a hundred million dollars each to Indonesia and Thailand. Since the start of our more aggressive program in September 1985, we have made offers of grants or soft loans on twelve individual transactions in eight countries. U.S. exporters have won five of these cases, one has been lost and six are in various stages of review by the borrower. I am convinced that our more aggressive attitude, as demonstrated by these offers, helped establish the negotiating climate which made agreement possible. But as I mentioned before, the full force of the tighter rules won't take effect until July 1988. Thus, we cannot consider the problem of mixed credits as having been completely solved. We will continue to meet mixed credits with war chest funds and vigorously pursue the fight to reduce export subsidies by other countries.

Now let's turn to numbers:

FY 1988 Budget Request

To carry out its programs in FY 1988, Exim is requesting:

--- a limitation of $1 billion for regular loan obliga-

tions, of which up to $200 million may be available as tied aid credits. In light of the current balance of $4.5 billion in outstanding Preliminary Commitments, the additional $2.6 billion in applications for Preliminary Commitments and the anticipated average $300 million in medium-term loans, we think such a limitation is reasonable.

--- an appropriation equal to the grant element of tied aid credits made available, but not to exceed $200 million; such appropriation to be included within the $1.0 billion proposed for regular loan obligations.

--- a limitation of $10 billion for guarantee and insurance commitments; and

--- a limitation of $20.668 million for administrative expenses.

Under the Administration's credit reform proposal, the subsidy associated with agency loan or guarantee programs will be appropriated and serve as a limit on the amount of credit support which can be extended in a given fiscal year. As each loan or guarantee is approved, the applicable subsidy will be determined and charged against the subsidy appropriation.

For FY 1988, Eximbank is requesting a subsidy appropriation of $105 million on the $800 million of loans requested and a subsidy appropriation of $589 million on the $10.0 billion of guarantees and insurance requested.

In recent years, Eximbank has operated at levels well below those set in the annual Appropriations Acts largely as a result of heavy debt service burdens by the developing countries which were major markets for U.S. exporters, an overpriced dollar and the general sluggishness of the international economy which has led to the postponement or cancellation of numerous projects. Estimating future needs is always more of an art than a science. Nevertheless, we believe that levels being requested for fiscal year 1988 are realistic and will enable us to operate a new Eximbank that will respond more vigorously and effectively than ever to the needs of the U.S. exporting community.

The Administration is also asking for up to $200 million to fund a "war chest" for use in connection with tied aid credits. We believe such funding is necessary even though we have reached agreement on new guidelines because they do not become fully effective until mid-1988. Moreover, even with the new guidelines in effect, numerous prior offers may be "grandfathered." We intend by judicious use of the "war chest" to minimize the opportunities presented to our competitors by the fifteen-month phase-in period. For these reasons, we consider it important to be able to counter predatory practices of our competition throughout fiscal year 1988.

The administrative expense budget of the Bank provides funding for personnel, support services, and operating expenses. For FY 1988, the Bank is requesting $20,668,000

for administrative expenses which will support a full-time equivalent personnel level of 345. This is only six above the personnel level for FY 1987 and 20 percent less than for FY 1980.

Of the $20,668,000 requested, $15,677,900, or 76 percent, is for compensation and benefits, and $2,108,400, or 10 percent, is for rent of office space. Of the remaining expenses, travel is budgeted at $360,000, $54,000 is budgeted for needed marketing assistance which will be used to help reach new exporters, especially small business, and $18,000 is budgeted for official reception and representation expenses. The remaining balance of $2,449,700 will be used for necessary operating expenses such as telecommunications rentals, purchases of supplies, support services, equipment maintenance and an expansion of the information management resources of the Bank.

Operating at a level of 345 full-time equivalent personnel in FY 1988 is the minimum level that will allow the Bank to continue to analyze and process all new applications in a timely manner, maintain its debt collection activities at an acceptable level, properly monitor its existing portfolio, manage its claims and rescheduling workload, and sustain other necessary functions of the Bank.

The President has made it clear that exporting is a national priority; Eximbank has a vital role to play in ensuring that this priority becomes a reality. Through our own efforts as well as through cooperation with commercial sources of financing we can take a giant step toward restoring the competitive edge to American exports.

Thank you. I will now be prepared to answer any questions that you or the members of the Subcommittee may have.

COORDINATION OF U.S. EXPORT FINANCING PROGRAMS

Senator KASTEN. John, thank you very much.

In the bipartisan spirit of this committee, Senator Mikulski, we will begin with questions from you.

Senator MIKULSKI. Thank you very much, Mr. Chairman. I just have a few.

Mr. Bohn, can you tell me what the Eximbank is doing to develop a coordinated export financing policy with OPIC, TDP, AID, and USTR?

As a new Senator, I see this array of agencies that are supposed to enhance exports. Can you tell me where you fit in, and how that is working?

Mr. BOHN. Sure, I will be happy to, Senator.

Let's start with the one with which we work the closest, and that is TDP. The way that works is that TDP's responsibility is to search out situations where by providing a research grant or a feasibility study grant, we hope to get in on the ground floor as a country, so that when the follow on project takes place, we will have an inside track for American companies.

We work very closely with them. Often, for example, they will study a project, and we will then provide financing, or a financing offer, in support of U.S. exports for the project that comes thereafter. We have done three or four of these. We are involved in a coastal project in Turkey. We have been involved in a number of these kinds of situations.

In China, for example, TDP provided a series of grants, and in each of those cases, we wrote to the grantee indicating our interest, even before we saw the project, that if it turned out that this was a feasible project the Eximbank would be prepared to seriously consider the financing.

So what you have is a situation where they do the front-end work on a grant basis, which is very important because a lot of our competitors do that, and we try to follow along with the financing for the equipment needed. Again, the problem here comes back to this concessionary aid-type financing, which is often provided by other governments, but we do the best we can.

With respect to OPIC, they typically deal with investment, so there is no direct correlation in terms of the things that they do and we do, except that we might provide financing either in terms of direct credit or insurance or guarantees for the supply of U.S. products and services that would go to an investment project.

OPIC, from time to time, will lead investment missions, and from time to time, we will go with them to kind of present a united front.

With respect to the USTR, we find ourselves in the position, particularly as it relates to the Japanese, of trying to work with them in a number of market areas. I had a fair amount of experience in Japan over the years. I lived there for 4½ years. We have a number of mutual interests.

What we have tried to do, for example, as a result of discussions that USTR and other parts of the government have had, is to work with the Japan Eximbank and OECF to make available to American companies some of Japan's recyclable surplus. As a matter of fact, we have a staff officer over there trying to work out the mechanics.

The Japan Eximbank and OECF have both agreed to make these funds available on an untied basis. Our point to them was that nobody will believe that until American companies start getting business. They understand that, and they are prepared to do that.

What we get for American companies is access to some of those funds, and what we hope they get is credibility because we can work with them and with American companies to make sure that American companies get a shot at those funds.

In summary, that is the way it works. It is different in each situation.

EXIM-AID COOPERATION

Senator MIKULSKI. You also will consult with AID. I know that you were talking about selling big airplanes and big power projects. Sometimes, we have all been criticized for selling countries things they don't

need at prices they can't afford, and incur a debt that they could never pay back. I don't think that any of us are interested in that.

AID is in the field, hands on, particularly in some of the developing countries like the Philippines, or whatever. I wonder if you also consult with them as to whether it is a good idea to be moving with some of these guarantees into a particular country and a particular project?

Mr. BOHN. I think, Senator, that we will talk to them, but we are an essentially different business than AID. Having spent some time in the development side of finance, perhaps I am more acutely aware of it than others.

We do consult with AID. Where we consult most often is in those situations where a mixed credit or a tied aid credit is involved. We will ask them to participate and provide funds in support of American companies, to bring down the cost to the recipient country.

Analytically, at least, we would be the worst offenders in terms of doing just what you said. We do not look at essentially the purpose or the relevance or the suitability of a given export.

Senator MIKULSKI. You don't?

Mr. BOHN. We don't look at it as a primary exercise, and the reason for that is quite simple. That is not what we consider our job to be. In practice, you look at it because if a country is saddled with a whole series of projects that won't pay back, or will break that country's back in terms of debt service, then they no longer represent reasonable assurance of repayment.

So we have to look at it the other way, but we don't start in with a process of whether or not a particular requested import is developmentally suitable.

Senator MIKULSKI. I didn't mean developmentally suitable, but whether, exactly what I said, we sell products they don't need at prices that they can't afford and incur debt that they can't pay back. This is a concern.

Mr. BOHN. What we try to do, to the extent we can, is to stay out of that inquiry, because in most cases countries will know what they need better than we will, and we get into kind of an arbitrary situation, such as a popcorn machine might not be suitable and a road grader would be suitable. That tends to discriminate against certain kinds of exporters.

We tend to stay out of that except for the reason that I mentioned, namely, we will look at it in terms of the overall economy of that country, because if a country has too many popcorn machines and not enough road graders, it won't be able to pay either for the popcorn machines or for the road graders. So we look at it on an economic basis in terms of the capacity of that country to pay.

Senator MIKULSKI. Mr. Chairman, I have some other questions, but I will come back, because I know the time is of interest.

Mr. Bohn, if I could just say one thing. First of all, thank you. It gives me a sense of coordination. I know that you get higher marks than some predecessors. You don't have an easy job, and we could

spend all day just digging away, but I am pleased to see that at least there is an attempt at coordination.

Senator KASTEN. Senator D'Amato.

EXPORTS TO EGYPT

Senator D'AMATO. Mr. Chairman, I just have one question.

I am wondering, I see in your testimony that in the Middle East the largest buyers are Algeria and Tunisia. Could you tell me why Egypt, which has the largest aid program of the Arab world, is not among the leaders of U.S. imports associated with the TDP feasibility studies?

Mr. BOHN. Senator, I don't know that I can answer the question with respect to TDP feasibility studies.

What I can say is the following: Egypt has had some financial problems, which they are in the process, I think, of rectifying. They have gone to an IMF program. They are beginning to get rid of some of the subsidies that have distorted their economy.

My hope is that, over the next couple of years, the credit worthiness of Egypt will increase. The business that we have done in Egypt has been largely in the medium-term kind of exports. We have done some projects, but not all that many.

Egypt has a number of other sources of funds. For Egypt our cost is probably higher than funds they get, for example, under aid programs and the rest, and we suspect that that is largely responsible for the distortion.

Senator D'AMATO. Thank you, Mr. Chairman.

EXIM FINANCIAL POSITION

Senator KASTEN. John, I want to talk about the financial situation for a second. The Bank is supposed to report to Congress when the capital stock and the retained earnings fall to 50 percent of the balance as of September 30, 1983.

There was a GAO report released in May of this year saying that if the Bank had been following generally accepted accounting principles, the Bank would have had to notify the Congress as early as 1983 regarding its weakened capital position. The GAO report also said that even using the Bank's liberal accounting practices, the Bank projected 1987 losses would clearly mandate a report to Congress on the Bank's deteriorating capital position.

When will you make, if at all, the report to Congress, and what are your views as to the recapitalization of the Bank?

Mr. BOHN. Barring a sudden windfall profit from someone, we will probably be required to make that report in the first quarter of next year, which would be fiscal year 1988. Our estimate now is that we will get down to about $336 million at the end of 1987 and, as I said, in the first quarter of 1988, we will have to make that report.

This is a very serious question, and if I can, Senator, I would like to spend just a couple of minutes with it.

Senator KASTEN. Let me, if I can, add one additional question, and then you can cover it all together, because it is related, the problem loans.

According to the GAO's analysis, the problem loans are more than six times greater than the Bank's earnings. That fits in with this overall question, I just didn't want to ask two questions. You can just respond to kind of the whole package here, if you will.

I am reminded that the people in the back of the room are having a hard time hearing you, so you are going to have to apologize to them, and also speak up.

Mr. BOHN. I apologize to you all. I just didn't want to shout at you across the table.

LOAN LOSS RESERVE

There are two issues here, really. One is the GAO report, whose genesis is really a question of the appropriate accounting procedure and whether or not we should create loan loss reserves. Let me try to deal with that issue first, because it is related, but, I would submit, separate to your broader question on recapitalization and problem loans.

Every year since I have been at the Bank, the GAO has gone through and said that we should create a loan loss reserve. They go through and look at various countries, and come to a conclusion that the likelihood of repayment is something less than 100 cents on the dollar, and then they create a series, in my judgment, of speculative kinds of numbers.

They are proceeding, I submit, Mr. Chairman, from an erroneous premise, and the erroneous premise is that somehow if it is good for the private sector, it is good for the government. The point I make to them, and the point that I would like to make here, is that the reason you have loan loss reserves in the private sector is because you have investors to be concerned about, you have creditors to be concerned about; and in the case of banks, you have depositors to be concerned about.

As a government agency, we are responsible to the Congress and we report to Congress. Indeed, Congress has access to any piece of information that we have with respect to the quality of our loans. We go through in elaborate detail in our financial statements and comment on these.

As a matter of practice, if we were to provide a governmental judgment on the quality of a given loan, it is more likely than not to create the same kind of a problem that you are hearing now with respect to a country like Brazil wherein yesterday's paper indicated that since you wrote off some of the principal, why not make the loans at no spread.

Our concern is twofold. One, if we pass a judgment that a given country is unlikely to pay at 100 cents on the dollar, that could not be kept secret. It would then get into the marketplace and be apt to interfere with any kind of adjustments processes that are going on in some very elaborate and sensitive negotiations.

Secondly, if we were going to make such a judgment, it is essentially arbitrary, just as the judgment of First National City Bank was ar-

bitrary, but represented a decision between a management and its shareholders.

One the one hand, we have an arbitrary and, I would say, foolish argument in favor of consistency. On the other hand, I think we have some serious diplomatic problems that would result if an American government agency did, in fact, start passing judgment and those judgments got out.

"PROBLEM LOANS"

Senator KASTEN. What you are saying then is that you disagree with the GAO analysis as to the definition of a so-called "problem loan." Is that what you are saying?

Mr. BOHN. I disagree with the GAO position that it is appropriate for the Export-Import Bank to get into the business of loan loss reserving.

Senator KASTEN. I understand that. But do you disagree with the definition of a so-called "problem loan" that the GAO was using when it said "problem loans are more than six times the Eximbank's earning"? The problem is their definition of problem loans; is that what you are telling us?

Mr. BOHN. The problem is that their definition of problem loans is no more accurate than anybody else's definition of problem loans. If you took a dozen bankers and sat them in a room, or a dozen accountants and sat them in a room, you would get at least a dozen different valuations of what problems loans were.

Senator KASTEN. Based on your track record, can you say that the ones that they call "problem loans" are, in fact, turning out okay, and you are getting repaid; or are we just building up an ever growing group of loans whose definition we are going to quarrel about?

Mr. BOHN. I don't think——

Senator KASTEN. Are the GAO problem loans not turning out to be problems?

Mr. BOHN. No. I wish I could say that they were not problems. Clearly, the problem loans, however defined, have been increasing, and probably over the short term will increase again. We take the position that our entire capital and reserve, such as it is, are reserves for problem loans. To take the position of passing judgment on any given country has some significant adverse political effects and no real positive benefits.

We will concede, in terms of loans that are not performing or are performing badly, and we can go down and pick countries that are not paying—I don't want to say that all of our loans are getting better, that is not the case. The question, as I understand it from GAO, is an accounting one: what is the suitable way to report.

My point here is that this is a function of information necessary for oversight, and I have never found the situation where any part of the Congress didn't feel they understood, for oversight purposes, what our loans were and what we were doing.

Senator KASTEN. We have some other questions on this issue that we would like to submit for the record so that you can help us in this area.

Mr. BOHN. Sure.

Senator KASTEN. Senator Mikulski, do you have any further questions for Mr. Bohn.

Senator MIKULSKI. No. Actually, Mr. Chairman, your questions followed along some of the questions I had.

BUDGET USAGE

Senator KASTEN. For the last 6 years, we have actually provided—You address this in part in your testimony—more funds than you have been able to use. During this time of tight budgets, providing those funds has been tough for us as appropriators. At the same time, you haven't used the money.

Why have these carryovers occurred, and are you confident that your request this year is at the appropriate level and that you will, in fact, use the money that Congress will appropriate?

Mr. BOHN. Mr. Chairman, I was confident about last year's level, so my track record is not very good.

Senator KASTEN. Some of us are always trying to prompt you to do a little bit more in terms of helping export. We are now at 75 percent.

Mr. BOHN. We have looked at this in every way we can. I believe that we will use the money requested. I think that it is likely, given the increase in volume over the last few months, that the amount of direct credit requested will be used.

Again, I have to add the caveat in terms of the interest rate function. We will use more financial guarantees if the interest rates stay low. If the interest rates go up, such that the value of the subsidy increases, then we will use more direct credit. Our belief is that, given the new programs, given what we see, some important adjustments in some of the Latin American countries which I think will increase demand, we will use it.

RECAPITALIZATION

Mr. Chairman, I never finished the last part of your question on recapitalization. Do you want me to go back to that?

Senator KASTEN. You said that we were going to be coming back probably in January of 1988 for recapitalization. Please touch on that very briefly.

Mr. BOHN. The one point that I would like to make here because it goes with the loan loss reserve issue as well, is that we can operate legally with a negative equity situation. I think that is a highly undesirable situation.

Senator KASTEN. Will a major appropriation be required to recapitalize the Bank in January of 1988?

Mr. BOHN. We have looked at this issue and we have developed three alternatives, two of which would require a major appropriation.

The third is the one that I think we will recommend, but we are still having discussions with OMB and the Treasury on this. We can refinance the Bank, that is to say, we can prepay our high rate borrowings and refinance at the current rates, eliminate the deficit at no im-

pact on the budget at all, if we are permitted to prepay the loans that we have without penalty.

Here is an area where the GAO and we agree. We are assessed, or would be assessed, on a refinancing a prepayment penalty by the Treasury Department, which would essentially amount to approximately $2 billion. There is no impact on the budget of this prepayment penalty. It is simply an internal governmental accounting entry. Neither GAO nor I, nor the staff at the Bank, can see any particular reason to do that.

If we are permitted to prepay, we can then eliminate these deficits, which I think will give a much clearer picture in terms of current operations. I worry a great deal about operating with negative equity. I think that it provides the wrong atmosphere.

Senator KASTEN. Therefore, do we anticipate a major appropriation in order to make sure that you are not? What are you saying? If you don't want to operate with negative equity, what do we have to do?

Mr. BOHN. Permit us to prepay or refinance our existing debt without that prepayment penalty, which as I said has no impact on the budget at all. It is a series of internal governmental accounting entries. That, then, requires no appropriation; otherwise we will have to come to you and either request an appropriation to recapitalize the Bank, or a make conscious decision to operate with negative equity.

MIXED CREDITS

Senator KASTEN. Let me just ask a quick question on mixed credits. There are some people who are arguing that if we have a mixed credit program, which we will have in the trade bill and we establish a strong mixed credit program, the so-called "war chest," additional direct loan authority is not necessary.

Are mixed credits and direct loans complementary or do mixed credits, in your opinion, substitute for direct loans?

Mr. BOHN. One is a subset of the other. A mixed credit is a kind of direct loan. It is a loan made by an export credit agency which is "mixed" with aid. The better way to think about it is simply the concessionality level of that loan. We make a direct loan according to the consensus and the concessionality level cannot be more than 30 percent. If it is more than 30 percent, it is, in fact, aid.

So whether it comes from the Export-Import Bank, or whether it comes from the aid agency and, therefore, is called a mixed credit, is really not of great importance, but they are all direct loans. The direct loan program is required in order to have a mixed credit program.

EXIM DEBT PREPAYMENT

Senator KASTEN. Going back to the other question, do you need legislation to prepay without penalty? Do you need some kind of permissive legislation, or can the Treasury Department simply say that you can do it? What do you need in order to prepay, if we, in fact, want to work with you in that way?

Mr. BOHN. We have asked Treasury. The lawyers say that this is not subject to waiver by the Secretary, so we would need legislation.

Senator KASTEN. Theoretically, you would need legislation in this appropriations bill.

Mr. BOHN. Yes.

Senator KASTEN. So you are looking to that for next January, assuming that we are going to be in a continuing resolution, or some kind of bill this fall?

Mr. BOHN. Yes.

Senator KASTEN. Let's work together with Senator Inouye and others to try to find out whether we ought to move in that direction, working with you and your lawyers.

Mr. BOHN. We will be happy to submit our information to you, Senator.

Senator KASTEN. We have a couple of other questions having to do with the use of mixed credits and standards that I think, in the interest of time, we probably ought to save, and move on to other witnesses. Let me just say thank you for the opportunity to work with you, and we hope that you are going to get above 75 percent.

Mr. BOHN. So do I, Senator, so do I.

Thank you all very much, and I would like to thank this committee for its continuing support.

Senator KASTEN. Thank you very much.

AGENCY FOR INTERNATIONAL DEVELOPMENT

BUREAU FOR LATIN AMERICA AND THE CARIBBEAN

STATEMENT OF MR. IRWIN A. LEVY, DEPUTY DIRECTOR, OFFICE OF DEVELOPMENT RESOURCES, BUREAU FOR LATIN AMERICA AND THE CARIBBEAN, AGENCY FOR INTERNATIONAL DEVELOPMENT

INTRODUCTION OF WITNESS

Senator KASTEN. We are going to combine Mr. Levy and Mr. Holmes as one panel, and then we will hear from Mr. Nalen.

Our first witness in this group is Mr. Irwin A. Levy, the Deputy Director of the Office of Development Resources, Bureau for Latin America and the Caribbean, and the A.I.D. Trade Credit Insurance Program. Mr. Levy.

Mr. LEVY. Thank you, Mr. Chairman.

Senator KASTEN. I will remind you of the same thing that I reminded Mr. Bohn about, the people in the back of the room have a hard time hearing you.

TRADE CREDIT INSURANCE PROGRAM [TCIP]

Mr. LEVY. The Trade Credit Insurance Program is a rather atypical program for A.I.D. It grew out of the recommendations of the Kissinger Commission. The purpose was to try to induce U.S. commercial banks to return to their previous credit role in Central America.

The program provides guarantees for financing transactions involving the exports of goods and services for the use of the private sector in Central American countries. It operates in four countries—Guatemala, Costa Rica, Honduras, and El Salvador.

Under this program, U.S. commercial banks open lines of credit to banks in these countries, and the obligations to repay these credits are guaranteed by either the Central Bank of the recipient country or the full faith and credit of that country.

The banks that provide these credits are insured by Eximbank, which in turn is guaranteed against loss by A.I.D. The program was set up in a way to minimize the administrative burden for both Eximbank and A.I.D. When you talk about coordination, we have worked very closely with Eximbank in a very satisfactory way, and it has been really a pleasure. It has been determined that we would utilize Eximbank's regular procedures to the maximum extent possible so as to minimize the burden on us and the burden on U.S. banks who are familiar with these procedures.

TCIP CRITERIA

The criteria for the program are very few. The program is supposed to fund imports from the United States that are repayable in 12 months or less. The imports are for productive purposes in the private sector, and to the maximum extent practicable for export industries, and no defense articles or services are permitted.

We have set up a reserve fund for the possibility of paying any claims under this program. Twenty million dollars has been obligated for this so far, but in fact no claim has been presented against the program and no payments have had to be made.

UTILIZATION RATE

As with many programs that A.I.D. is familiar with, it did not get off to a very fast start. This is not unusual. Programs in lesser developed countries frequently have long gestation periods. I guess the program has still not achieved the rate of utilization that we anticipated when it was created. But I think it is fair to note that as of the end of May there were a total of $266 million in letters of credit that had been confirmed under the program.

I mention in my prepared statement that the program utilization rate, we hope, would increase in Costa Rica and Guatemala. In fact, I learned yesterday that in Guatemala, letters of credit issued during June totalled $1.3 million, compared to a utilization rate in the previous month of less than $200,000. So there has been a significant increase in Guatemala, and whether it will continue, I don't know.

EL SALVADOR

To finish this brief exposition of the program, I would like to refer to a comment by our El Salvador Mission in terms of their appreciation for what the program has achieved. They reported that as a result of the program, $38 million in collateral deposits that Salvadoran banks were previously required to keep were freed up and interest rates on their credits were reduced by up to 3 percent.

Indeed, the Salvadoran banks were able to utilize this insured credit as leverage to obtain lower interest rates on additional credit which was not guaranteed under the Trade Credit Insurance Program.

In sum, we think that the program has incurred minimal costs, and certainly a very minor administrative burden for A.I.D., and we believe for the Export-Import Bank. No claims have been paid, and it has achieved significant benefits. For that purpose, we are seeking continuation in fiscal year 1988 at the $200 million guarantee level.

Senator KASTEN. We thank you for your statement.

(The prepared statement follows:)

PREPARED STATEMENT OF IRWIN A. LEVY

DEPUTY DIRECTOR

OFFICE OF DEVELOPMENT RESOURCES, BUREAU FOR LATIN AMERICA, AND THE CARIBBEAN AGENCY FOR INTERNATIONAL DEVELOPMENT

Mr. Chairman, thank you for permitting me to say a few words to this subcommittee on behalf of the Trade Credit Insurance Program, or TCIP.

This program grew out of the report of the Kissinger Commission which recommended the creation of the TCIP as a means to induce U.S. banks to return to their previous credit role in Central America. It is authorized by Section 224 of the Foreign Assistance Act of 1961, as amended, which permits guarantee commitments to be entered into until September 30, 1989.

The TCIP provides guarantees for financing transactions involving the export of goods and services for the use of the private sector in Central American countries. Under this program, lines of credit are opened between commercial banks in the U.S. and banks in four Central American countries—Guatemala, Costa Rica, Honduras, and El Salvador—with the obligation to repay guaranteed by either the central bank of the recipient country or the full faith and credit of that country. This credit is insured by Eximbank, which, in turn, is guaranteed against loss by A.I.D. The program was set up to operate as simply as possible so as to minimize the administrative burden for Eximbank and A.I.D. and to induce the maximum participation of U.S. commercial banks by avoiding unnecessary paperwork. Accordingly, A.I.D. and Eximbank determined to utilize Eximbank's regular procedures and practices to the maximum extent possible. The criteria for the program are few: the program is available to fund imports from the United States, repayable in twelve months or less; the imports are for productive purposes in the private sector and, to the maximum extent practicable, for export industries; no defense articles or services are permitted. These criteria were spelled out in agreements signed by A.I.D. with Eximbank and with each of the participating countries.

A total of $300 million in guaranty authority was authorized for FY 1985; $250 million for FY 1986; and $275 million in FY 1987. For FY 1988 the Administration is requesting authority of $200 million.

As mandated by the authorizing legislation, A.I.D. has established a reserve fund for the program. To date, $20 million has been obligated for this reserve by agreement between A.I.D. and Eximbank. Absent a major increase in program utilization, or adverse claim experience, we do not anticipate the need for additional reserves.

The program got off to a rather slow start, which is not atypical of new programs being initiated in lesser developed countries. But by March of 1986, a total of $60 million in letters of credit had been confirmed under the program. By May of this year, that figure had risen to a total of $266 million. The total of guarantees outstanding (which are the total of letters of credit issued minus letters of credit liquidated) has been running at approximately $79–$82 million. There is some indication that the program utilization rate will increase in both Costa Rica and Guatemala during FY 1988.

I would like to make several points about the program:

(1) While it has not been utilized to the maximum permitted by our authority, it nevertheless has been utilized to a considerable degree, as the figures I have quoted above show.

(2) The program has proved beneficial. For example, our Mission in El Salvador has reported that, as a result of the program, $38 million in collateral deposits were freed and interest rates were reduced by up to 3 percent. El Salvador found an enthusiastic response to the program from foreign banks and leveraged the insured credit with an additional 25 percent of uninsured credit with concessional terms. We do not have similar information with respect to the program in other countries, but we anticipate that the full evaluation of the program scheduled for early in FY 1988 will show similar benefits in the other participating countries.

(3) These benefits have been achieved at a minimal cost. A.I.D.'s administrative burden has been slight, and there have been no claims, to date, under the program.

The Administration is requesting, for FY 1988, $200 million in guaranty authority for this program. We believe that the benefits of the program, achieved at minimal cost, merit its continuation.

Thank you very much.

U.S. TRADE AND DEVELOPMENT PROGRAM

STATEMENT OF CHRISTIAN HOLMES, DIRECTOR, U.S. TRADE AND DEVELOPMENT PROGRAM

INTRODUCTION OF WITNESS

Senator KASTEN. What I would like to do is to ask Chris to make his opening statement, and then we might ask questions of both of you.

Chris Holmes, the Director of the U.S. Trade and Development Program, and we look forward to your statement.

Mr. HOLMES. Thank you, Mr. Chairman and Senator Mikulski.

I have a prepared statement which, with your permission, I would like to have in the record.

Senator KASTEN. Without objection, it is so ordered.

Mr. HOLMES. I would like briefly to describe what we are doing and what some of our results have been, and where we think we are going.

BUDGET REQUEST

For fiscal year 1988, we are requesting $20 million to carry out the objectives of the Trade and Development Program. Our principal objective is to promote trade and U.S. exports to developing countries in such a way that it also fosters economic development in those countries in which we operate.

We try to achieve that objective by financing planning services, feasibility studies, and related activities on projects in developing countries that could use U.S. goods and services in the design and in the construction and in the equipping of a project.

FOUR WINDOWS OF OPERATION

We basically operate through four different windows. One window finances feasibility studies on large scale infrastructure projects in developing countries like a dam, or a power station. The second window finances technical assessments of the deposits of strategic minerals and metals in developing countries on which we are potentially dependent. The third window finances conferences and limited training centered around projects that we are trying to tie down for U.S. exporters.

These three windows together comprise about 90 percent of our project funds. The fourth window is our investor window where we cost share feasibility studies with U.S. investors on projects in developing countries. This window is really our high risk window and it is where we operate in countries that are very difficult to operate in in terms of our normal TDP program.

PROGRAM RESULTS

In terms of our results, as of last Friday, we have obligated since fiscal year 1981 some $82 million on a total of 454 projects covering some 74 countries. I might note that we have done that over a 6-year period when we have taken our staff from some 30 people down to 18, and have roughly kept our operating expenses at the 10 to 12 percent level, which is becoming increasingly difficult as the program has grown significantly over the last six years.

We believe that the funds that we have obligated to date have generated approximately $800 million in exports from some 53 cities.

Senator KASTEN. Did you say $800 million?

Mr. HOLMES. Yes, $800 million. We have had two independent audits to look at those figures plus some friends on the committee staff are coming downtown to look at our figures also. We feel pretty confident with that.

As to the future, the real question for us is: Do we continue operating on the past strategy which has been pretty successful? We have concluded that in terms of the first three windows, where we have had the bulk of our successes, that is the big infrastructure projects, the minerals, the conferences, we are going to go ahead with the same strategy.

The fourth window has been the more complicated window, and this is where we take a big risk, where we go one on one with an American investor who wants to do, let's say, an agribusiness project in the Island of Dominica in the Caribbean, which is not exactly a place that is attracting a great deal of investment, and we would like to have more go there.

FEASIBILITY STUDIES

We have done some 80 feasibility studies, about 50 of those are still live, where investors are trying to put together syndicates. It takes maybe 5 years to finally put together a syndicate to get capital into a project. But to date, of those 50, only about three that we can tell, three to five, have actually gone ahead with investments. Within those 80, we seek reimbursement if the investment goes forward, and we have gotten reimbursement on three.

So for this year, we started to drop the number of those investor studies. Last year, we did 22, but this year we will only do ten or eleven. In fiscal year 1988, we are not really quite sure how many investor studies we are going to do, because we are going to look at the past.

I would like to give you just one example of where the program has really worked well. What we try to do is to bring these windows together so that they operate interactively so that we build value in the four different windows.

TAIWAN PROGRAM

We began a program in Taiwan a year-and-a-half ago because of the tremendous surpluses that they are amassing, to some extent at our expense. A member of your committee, plus a number of other Members of Congress wrote the Taiwan authorities and said: Look, we want

American firms to get a piece of the big rapid transit projects that are going on in Taiwan.

We financed a feasibility study—that is one window—in Gaoshun, which is one city where they are going to spend part of $5 billion in rapid transit. We financed a conference to bring together equipment suppliers. We financed a limited amount of training, where we brought the Mayor of Taipei over to the United States to take a look at our technology.

The Mayor, in turn, returned to Taiwan to make the decision on a $50 million engineering contract to design, basically, the future for the use of U.S. goods and services, hopefully, in Gaoshun and in Taipei. He went ahead, and this is really interesting, and took a look at all the different analyses, and made the go sign to give a U.S. consortium a $50 million follow-on contract, and that was based on $1 million of combined activities by TDP over a year-and-a-half.

I think that we are getting better at what we are doing. I think we recognize where we are taking some big risks. We have been working very closely with your staff, for which we are grateful.

This is the sum and total of what we are about.

[The prepared statement follows:]

PREPARED STATEMENT OF CHRISTIAN HOLMES
DIRECTOR
U.S. TRADE AND DEVELOPMENT PROGRAM—AID

Mr. Chairman, Members of the Subcommittee:

Thank you for this opportunity to testify in support of the Administration's Trade and Development Program (TDP).

The U.S. Trade and Development Program (TDP), a component agency of the International Development Cooperation Agency, is the principal organization in the U.S. Government which uses foreign assistance funds to increase U.S. exports. It does so by financing the planning of projects in developing countries that have significant potential for using U.S. goods and services in the design, construction, and operation of the project. This planning assistance also makes a contribution to the economic development of the countries in which TDP operates.

For FY 1988, the Administration is requesting $20 million to support TDP operating and program expenses. This amount will enable TDP to leverage foreign assistance funds for the benefit of American workers and developing countries alike. Our request will also enable us to continue to concentrate on areas of high priority to your Subcommittee, such as increasing trade and investment in the Pacific Basin.

The principal justification for our request is not just the need of developing countries and U.S. exporters for the services provided by the Trade and Development Program. Fundamentally, the justification is TDP's track record. In this regard, we have just completed an exhaustive evaluation, undertaken by an independent entity, on the impact of TDP studies on U.S. exports. Since 1980, TDP has obligated $75 million for feasibility studies and other planning services which will create major export markets for U.S. goods and services. The evaluation concludes

that TDP's feasibility studies since 1980 have been responsible for $605 million. In addition, $6.3 billion in exports are expected in the next 5 years and $5.4 billion are anticipated over the next 5-20 year period. (We believe that the evaluation is conservative as to actual exports generated to date and conclude that we have generated close to $800 million in exports.)

In my testimony today, I plan to concentrate on the impact of the TDP program on the U.S. economy. However, before doing so, I will provide the Subcommittee with:

-- an overview on the FY 88 budget request; and

-- a description of some successful TDP projects;

TDP FY 88 Budget Request

For FY 1988, the Administration is requesting $20 million to support the activities of the Trade and Development Program. TDP plans to continue its past strategy of assisting U.S. firms in capturing major export markets. Much of our work will concentrate on responding to commercial opportunities. However, we can also project with some certainty the following features of our FY 1988 program:

-- We will continue to pursue our Congressional mandate to operate in countries where the United States does not have bilateral assistance programs. We will be particularly active in China, Taiwan, Turkey, Korea, Colombia, and Argentina.

-- We also anticipate significant programs in Thailand, Zimbabwe, and the Philippines.

-- We will also carry out our Congressional mandate to develop natural resources of strategic interest to the United States. In this regard, we will concentrate on planning the development of titanium, chromite, manganese and cobalt deposits.

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-- We will continue our special initiatives, carried out in the past in close cooperation with representatives of Congress from the Pacific Northwest, to identify markets for U.S. wood products.

-- We will concentrate on generating both trade and investment in the Caribbean Basin and the Pacific Rim.

-- And, finally, we plan to keep our operating expenses at approximately 10% of our total program.

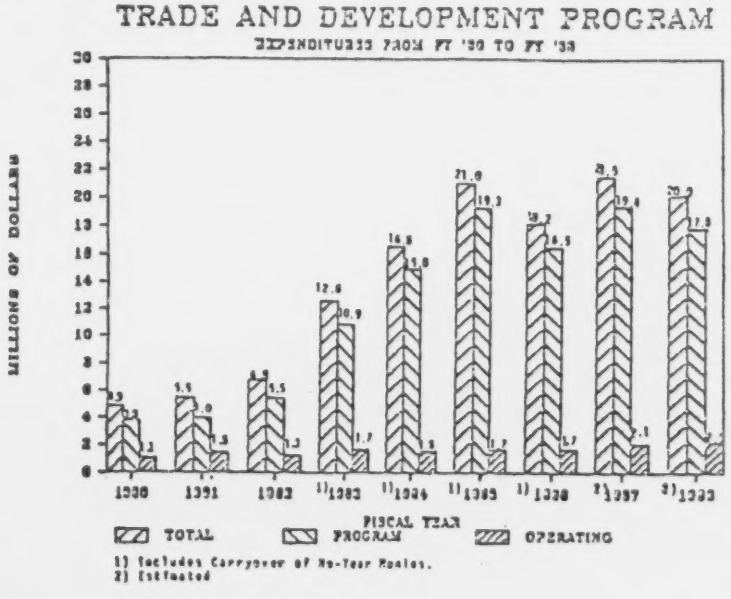
The following table tracks the growth of TDP.

TDP OBLIGATIONS
($millions)

	Fiscal Year							
	80	81	82	83 1/2/	84 1/	85 1/	86 1/	87 1/*
Program:	3.8	4.0	5.5	10.9	15.0	19.3	16.5	19.4
Operations:	1.1	1.5	1.3	1.7	1.6	1.7	1.7	2.1
	4.9	5.5	6.8	12.6	16.6	21.0	18.2	21.5

1/ This amount includes deobligations from previous fiscal years in which TDP had carryover authority.
2/ Includes $2 million from Department of Energy.
* Estimated.

As to operating expenses, the following bar graph depicts the relationship between TDP's operating and program costs. As the graph indicates, TDP's budget grew by 400% between 1981 and 1986. The operating expense ratio was reduced from 22% of the budget in 1981 to 10% of the budget in 1986.



Special Initiatives

In FY 1988, TDP anticipates funding special initiatives in strategic minerals and metals, in training and in wood products. These initiatives, detailed below, reflect TDP's ability to innovate, adjust to new commercial opportunities, and implement special features in its Congressional mandate.

-- Strategic Minerals & Metals: TDP is undertaking a special effort to identify sources of strategic minerals and metals in the developing world. This initiative was taken pursuant to statutory language in Section 661 of the Foreign Assistance Act of 1961, as amended, which authorizes TDP funds to be used to facilitate access to natural resources of strategic interest to the United States. In 1981, TDP identified a number of strategic minerals and metals for which the United States is particularly dependent on overseas resources. These included manganese, cobalt, chromite, and the platinum group of metals. Since then, TDP has analyzed the technical and economic feasibility of extracting strategic materials from Mauritania, Gabon, Madagascar, Morocco, the Philippines, Brazil, Turkey, Peru and Senegal.

TDP plans to send project teams to look at titanium deposits in Mozambique and chromite deposits in New Guinea. In FY 1988, TDP intends to fund a study in Madagascar on a ferrochrome mine and production facility.

-- Training: In FY 1986 and FY 1987, TDP financed a combined effort of U.S. businesses with community and junior colleges to identify and plan the development of major international training projects, such as vocational training centers in developing countries. These projects present substantial markets for U.S.

goods and services. By 1990, the World Bank will be devoting approximately $2 billion a year to financing training projects, and the TDP initiative is targeted in large part on helping U.S. firms capture a significant portion of these World Bank contracts. Already, TDP has dispatched teams to identify and help plan training projects in Indonesia, Malaysia and China. We attach a very high priority to this initiative, as it meets both a critical development need and helps open a new market for U.S. industry.

-- Wood Products: In an effort to identify and pursue markets for wood products, TDP has financed two major conferences, held in the Pacific Northwest, which have brought together officials from Latin America and Pacific Basin nations with U.S. Government officials and U.S. businessmen. In addition, TDP has financed project identification teams to help identify opportunities in specific nations for the export of U.S. wood products.

Successful Projects

The following are examples of TDP projects where U.S. exporters received significant follow-on contracts for goods and services.

-- Algeria Irrigation: In 1985, TDP provided a $46,428 grant to the American firm Western Agri-Management (Denver, Colorado). Western Agri-Management competed against firms from France, Italy and Spain to conduct a feasibility study on a major irrigation project. The TDP grant enabled Western Agri-Management to obtain the prime contract to provide some $30 million in equipment from the United States to support this project. Principal suppliers of the equipment were from Nebraska and Wisconsin.

-- Zhuhai Economic Zone: In 1984, TDP provided a grant of $161,777 to the People's Republic of China to enable

H.K. Ferguson Company (San Francisco, California) to conduct a feasibility study on an industrial zone in Zhuhai Special Economic Zone. One of the recommendations of the study was that a compressor factory be established. Based on that recommendation, the People's Republic of China purchased a $2.5 million plant from the United States.

-- Nepal Hydropower Project: One of the most important aspects of the TDP program is the ripple effect of the feasibility studies TDP finances. For example, in 1985 TDP financed a $650,000 feasibility study carried out by the firm of Morrison-Knudsen (Boise, Idaho) on a major hydropower facility in Nepal. Morrison-Knudsen conducted the study with a partner from the People's Republic of China. The Chinese partner was so impressed with Morrison-Knudsen's expertise on the Nepal project that the Government of China in turn awarded Morrison-Knudsen a $20 million contract for work in China. The TDP study thus gave Morrison-Knudsen significant contacts not only in Nepal but also in China to do work on projects which are of major development importance to both nations.

-- Thailand Power Projects: In some countries, TDP concentrates on a specific sector and a specific foreign government ministry because the sector will provide major markets for the export of U.S. goods and services. Such has been the case with TDP's work in the power sector with the Electric Generating Authority of Thailand. Since 1981, TDP has provided $5.4 million for 13 studies in the coal, power, and electrical transmission sectors. As a result of this work, some $30 million has been spent on U.S. equipment, primarily dump trucks (from the Terex Corporation and the Caterpillar Tractor Company). The U.S. firm, Med

Assistance and Performance Association, received a $1 million consulting and training services contract, and the American engineering firm of Dravo Van Houten received a $400,000 contract, for supervision of coal exploration efforts. In addition, the American engineering firm LEMCO has received some $20 million in a variety of engineering and consulting contracts.

Impact of TDP

As indicated previously, TDP has just concluded an extensive evaluation of TDP's track record in generating U.S. exports. We would be pleased to share this evaluation with members of the Subcommittee and staff. This evaluation was the second major evaluation undertaken on TDP projects in the last 18 months; in order to ensure that we are receiving an objective analysis, we have had different firms conduct these two evaluations. Interestingly, both evaluations reached very similar conclusions as to total exports generated to date and long-term potential exports. In addition to these evaluations, our staff is also in constant contact with TDP contractors on specific projects so as to determine the impact of our studies.

Essentially, our evaluation concludes that:

1) Approximately one out of three TDP studies have already produced or are expected to produce substantial U.S. exports.
2) On a pro-rated basis TDP has invested an average of $10 million a year in feasibility studies and other planning services; it has averaged an annual return of 86 million dollars in U.S. exports.
3) TDP's studies have been responsible for actual export of $605 million. In addition, $6.3 billion are expected over the next 5 years, and $5.4 billion could occur over the next 5-20 year period.
4) Subcontract activity resulting from TDP-supported projects will clearly involve a much greater number of

exports, including small and medium-sized businesses from virtually every state of the union.

5) Over 60 countries are involved in TDP projects, with 62% of actual exports going to Asia, 8.3% to the Middle East, 13% to Latin America, and 16.7% to Africa.

6) TDP's programs are clearly critical to a vast number of U.S. firms, highly productive in terms of their impact on U.S. exports, and a very necessary component of the overall U.S. trade development effort.

7) Over 200 U.S. firms have been, or are expected to be, major exporters in connection with projects resulting from TDP feasibility studies. These firms come from 34 different states. However, it should be noted that most of the exporters do their manufacturing in a number of plants located in different states and virtually all of them do extensive subcontracting with small, medium and large firms throughout the U.S.

Export Recipients

As shown in the table below, the exports generated by TDP feasibility studies have gone to a number of different countries around the world. The largest amount ($375.3 billion or 62%) has gone to the Asian countries. $101.4 million or 16.7% has gone to Africa, $78.9 million or 13% has gone to Latin America and $49.7 million or 8.3% has gone to Africa.

U.S. TRADE AND DEVELOPMENT PROGRAM
ACTUAL AND ESTIMATED TDP-GENERATED EXPORTS BY REGION

		Estimated Export Value (millions)		
	ACTUAL	5 YEARS	5-20 YEARS	TOTAL
TOTAL AFRICA	101.4	444.3	748.0	1,293.7
TOTAL ASIA	375.3	4,096.9	2,094.0	6,566.2
TOTAL LATIN AMERICA	78.9	922.7	505.8	1,507.4
TOTAL MIDDLE EAST	49.7	865.5	2,085.5	3,000.7
	605.3	6,329.4	5,443.3	12,368.0

In Asia, the largest country destinations for actual exports

are Thailand ($197 million), the Philippines ($118.3), China ($39.2 million), and Indonesia ($12.1 million). In the Middle East, (including East Europe), the largest buyers are in Algeria ($27 million, and in Tunisia ($13.2 million). In Latin America, the largest volume of exports proceeding from TDP feasibility studies is in Venezuela ($68.7 million). Finally, in Africa, the largest project is in Nigeria ($98 million). Clearly, the economic condition of some of these countries is a serious impediment to project fulfillment. The arrangement of satisfactory financing is one of the most important elements to achieve full U.S. export potential.

TDP's Export Sectors

TDP's projects have been well diversified by sector. In accordance with its charter, TDP has authority to encourage projects in the areas of energy development, food production, minerals development, transportation, communications, technical training, and other sectors of major priority to host governments and international development efforts. The actual and estimated exports resulting from TDP's feasibility studies are summarized below by sector:

U.S. TRADE AND DEVELOPMENT PROGRAM
ACTUAL AND ESTIMATED TDP-GENERATED EXPORTS BY SECTOR

	ESTIMATED EXPORT VALUE (MILLIONS)			
	ACTUAL	5 YEARS	5-20 YEARS	TOTAL
FOOD PRODUCTION	$132.7	$ 353.5	$ 518.8	$ 1,005.0
ENERGY DEVELOPMENT	246.4	2,130.7	2,302.0	4,679.1
INDUSTRY	123.5	739.2	571.0	1,433.7
COMMUNICATIONS	1.8	804.5	466.5	1,272.8
TRANSPORTATION	9.7	1,883.2	1,280.0	3,172.9
TRAINING	1.9	77.8	0.0	79.7
MINERALS DEVELOPMENT	13.3	197.0	215.0	425.3
OTHER	76.0	143.5	80.0	299.5
	$605.3	$6,329.4	$5,433.3	$12,368.0

TDP's Export Activity Growth

U.S. export potential from TDP support has shown strong and sustained growth since TDP's inception in 1980. This is reflected in the table below.

U.S. TRADE AND DEVELOPMENT PROGRAM
ACTUAL AND ESTIMATED TDP-GENERATED EXPORTS BY YEAR
JANUARY 1987

TDP FUNDING YEARS	ESTIMATED EXPORT VALUE (MILLIONS) ACTUAL	5 YEARS	5-20 YEARS	TOTAL
Total 1980	6.0	35.5	5.0	46.5
Total 1981	252.6	70.7	325.0	649.3
Total 1982	98.4	361.5	1,119.0	1,577.9
Total 1983	30.4	512.2	561.0	1,103.6
Total 1984	28.5	904.7	1,122.5	2,055.7
Total 1985	33.7	2,252.8	788.1	3,074.6
Total 1986	0.3	2,192.0	1,263.7	3,456.0
Total All Years	605.3	6,329.4	5,433.3	12,368.0

Included in the totals is $404 million of actual and potential exports resulting from pre-1980 USAID activity which was subsequently administered by TDP. It may be noted that actual exports are highest as they relate to TDP's feasibility studies of the earliest years. This is due to the long lead time between initial TDP approval of the feasibility study, the time it takes for the U.S. contractor to perform and deliver the study, and the sponsor's decision to proceed with the project, line up financing, start construction, and make its purchases from the U.S. The same factor reduces the amount of anticipated exports arising from TDP's 1986 feasibility studies, many of which are still underway.

Impact on U.S. Communities

TDP has had and will continue to have a far reaching impact on U.S. states and cities. Appendix A identifies states and cities which are either actual or potential exporters to projects for which TDP has financed feasibility studies and other planning services. We have deleted from these tables the company names, actual products being sold (or expected to be sold), and names of the TDP projects, as many U.S. contractors feel that our foreign competition would benefit from this information. We would, however, be pleased to share this information separately with the Subcommittee and staff.

In conclusion, Mr. Chairman, we would like to express again our thanks for your Subcommittee support of TDP's efforts to promote both U.S. exports and economic development in the developing world.

TRAINING

Senator KASTEN. Senator Mikulski.

Senator MIKULSKI. Thank you, Mr. Chairman.

Mr. Holmes, you have certainly given us a lot of activity for $20 million. It is refreshing.

Mr. HOLMES. Thank you.

Senator MIKULSKI. I have just a couple of questions. One is related to the issue of training, and see whether this is really what you do and whether it is the direction to go in.

Some of my exporters, like in dredging equipment or some others, say that when they go out to compete, they are competing with other countries, and often other Western industrialized countries.

Some of the ideas that they have talked about was that when we sell, say, industrial equipment, whether that is a Mack truck, a Caterpillar, dredging equipment, and so on, that we finance the training of the indigenous workforce in that country. That we are not going to get kickbacks, and we are not going to subsidize interest rates, and all those other things that other countries have given. It is not within the culture of our country to do that.

What do you think of the idea of using either your money, or through the kind of deals or arrangements that you put together, where they buy American equipment, we will provide the training of an indigenous workforce as a sweetener to do that? Either we train them here, or we go there, to do two things. One, make sure that we are building a working class in that society, a trained one; and, second, as a sweetener, to not only sell the initial product, but then have them keep coming back to buy that.

Is that something that you do, or you don't, but you think that it is a good idea?

Mr. HOLMES. I think it is a great idea. The problem would just be the amount of money that is available. We do some of it right now, but we do it on a very limited basis. I will give you an example of where we bring this training window that I have talked about and the feasibility study window together along the lines of what you are talking about, Senator.

We financed a feasibility conducted by Kaiser on a coal mine in China. We couldn't get the sale of the equipment following the feasibility study. So we brought some Chinese over to the United States. They went to New Jersey. They visited Ingersoll Rand, and they made a decision to buy $4 million worth of coal handling equipment, so it worked out. It was very limited training. It was about a five-week trip to the United States and very limited hands-on training.

Senator MIKULSKI. To do what I am talking about, what do you think it would cost?

Mr. HOLMES. A lot of money.

Senator MIKULSKI. A lot here is relative.

Mr. HOLMES. Okay. I should qualify that this, of course, is not in the Administration's request. I think, to have an impact on what you are doing, you would probably have to match, to some extent, what our foreign competitors do. Both the Canadians and the Japanese have very active programs in this area.

I would say, ballpark, to start off responsibly, to make sure that we could do what you are saying, rather than just grabbing the money, initially, I guess, in the range of $10 million.

Senator MIKULSKI. I would like you to do some calculations and come back to me and the committee on that. Then we can talk about this more precisely, or see if we would do some sector targeting. We don't necessarily have to do training to sell microscopes, if we are going to sell that, say, to China.

Mr. HOLMES. No.

SECTOR TARGETING

Senator MIKULSKI. But certainly dredging equipment to West African nations, Mack trucks, or whatever trucks, would need training. Also, I'd like to look at the idea of sector targeting.

[The information follows:]

TRAINING

With respect to training, TDP calculates that a pilot program of this nature would involve about $10 million. This would provide enough funding to have an impact in the area, but not excessive funding for the pilot effort. TDP does not believe that sector targeting would be an effective way to implement the program at this stage, because it is too soon to know which sectors will prove most productive. A reasonable number of sectors would be eligible initially, and targeting could be appropriate if several of the sectors show greater promise than the rest. Again, let me say that funding for a pilot program of this magnitude is not possible within the FY 1988 Administration's request for TDP. TDP would be happy to work with the committee staff if there are further questions.

STATE PROGRAMS

Senator MIKULSKI. The last thing is your fourth window, which obviously has some fog on it. I wonder, as you are exploring the way to use that, that instead of individual investor studies, essentially, in which we are doing feasibility studies for them, if we also took a look at some of the innovation that is going on in local communities.

There are now State programs. States are now formulating export initiatives. In some large urban areas, they are actually doing sister city projects. Apart from exchanging baseball bats, and things like that, they are actually doing some business on trade. For example, in my own State, we just took a trade mission, actually to Western Europe, but it could have been some place else, and we focused on biotech firms.

I wonder if, perhaps in your work, the State could come to you and say: This is the strength of our state, and we would like to export to some places. Could you tell us where we should go? Or something along those lines? Or a sister city.

I heard of a community in Hartford that is going to be selling telecommunications to a sister city in China. It is modest, but it was a medium-sized business in a city of that State. For Connecticut, it was big bucks.

Is this the idea of, if not the fourth window, maybe the lower pane?

Mr. HOLMES. We have been using a similar program as a windshield wiper, to use your metaphor. We have been experimenting. If I could take a minute or so to elaborate on this.

Senator MIKULSKI. We are looking at how to help local communities and medium-sized businesses.

Mr. HOLMES. We have been experimenting with how to handle the problem. The problem is that here we are located in Washington, so the people who can have the best access to our services, of course, are the people who can afford to have representation in Washington, or the States nearby.

We have been going out into certain States to take a look at the areas in which they have a competitive edge and then trying to provide conference type services, and stimulate trade missions, to be able to bring together the providers of equipment and the markets. So we are doing, to an extent, what you are discussing, and we want to do more.

Senator MIKULSKI. Our thinking is parallel.

Mr. HOLMES. Very much so.

Senator MIKULSKI. We need to work with people who are also developing a mobile infrastructure capacity, which you can't have, and can also provide evaluations for you in terms of what is the strength of a particular State.

Thank you, Mr. Chairman. I think those are the kinds of things we want. Mr. Chairman, I have no other questions.

UTILIZATION RATES OF GUARANTEE AUTHORITY

Senator KASTEN. Thank you.

Mr. Levy, if you look at your usage, El Salvador is above $150 million and all of the other countries are less than $50 million, going down to $9 million in Guatemala. Why has El Salvador been such a large user and is there an effort being made to try to increase your usage in Honduras, Costa Rica, Guatemala?

Mr. LEVY. The guarantee authority has been allocated so that, had the other countries been willing to use it, their utilization could have been at the same rate as El Salvador.

In other words, El Salvador has not been utilizing it more because they have been given a larger amount of authority. It has been a question of the extent to which the Central Bank, or the banks in that country have been willing or able to use it. I can't answer your question completely as to why El Salvador has utilized it freely, but I have some impressions.

First of all, I think, that the Central Bank in El Salvador, from all that I have heard, is the most capable central bank in Central America. They know how to utilize authorities that are available to them. They really were prepared, before anyone else, to start utilizing this program.

I think that to some extent in Guatemala there was delay in implementing the program because it was only after the new government came in that there seemed to be a seriousness in the Central Bank in starting to try to utilize this program.

Perhaps, they have now reached the point where their utilization will increase. As I said, the figures for June really show a remarkable increase.

Senator KASTEN. For Guatemala.

Mr. LEVY. In May, they utilized $104,000 in letters of credit, during June, $1.3 million. If that should continue at that rate, they would soon——

Senator KASTEN. There isn't any special bias that you have toward one country or another.

Mr. LEVY. Not at all.

Senator KASTEN. It is just a matter of what they are doing. Are you aggressively trying to help the countries that are using you less?

Mr. LEVY. Yes. Actually, in all of these countries, our missions spoke to the Central Banks and industries. Special programs were conducted to make people in the area knowledgeable of the program.

I remember sitting with people at the Export/Import Bank when they were doing a program by telephone, where our U.S. mission director had a number of Guatemalan businessmen in the room and people were asking questions about the program.

Just recently, the head of the insurance office that runs the program for Eximbank made a tour through Central America, again, to be available to clear up any problems and try to promote utilization, to the extent that the people were interested in utilizing it.

In all cases, the authority has become available to these other countries to the same extent as it has been to El Salvador. It has not been a program that we have deliberately skewed to one country.

FUNDING FOR FEASIBILITY STUDIES

Senator KASTEN. Chris, when you talked about the feasibility study of the export potential work, your evaluation showed that of the $7.8 million granted for the feasibility studies, $176,000 has been repaid.

Why is there such a low repayment level?

Mr. HOLMES. The 10 percent of the program is the window you are talking about. It is the only window where we try to get investment back. The answer why we do not get reimbursement is really very simple. It is that we can't go for reimbursement from these investors until they make the investment.

We are supporting efforts to make investments in a lot of parts of the world where such investments are high risk. What we are finding right now is that they are either making a decision not to go ahead and make an investment or they are taking a long time to make the investment. The court is really out because, as I said, about 50 of these studies are still either underway or have just been completed.

One thing we are doing, Mr. Chairman, to be prudent, is that we are cutting back on the numbers that we are doing. As we go into next year, we are going to make some really hard decisions as to what extent we use that window at all. We put Arthur Young under contract to go after all of them and find out where they are.

We have a target group that we are bothering, to say the least, to see how close they have come to making an investment and then to get it back.

SUCCESSFUL ASIAN PROGRAMS

Senator KASTEN. Let me just ask another question in terms of the return on your investments. Your evaluation showed an 8 to 1 positive ratio, but it also pointed out that your most successful projects are in Asia, and not a whole lot of successful projects are in Africa.

What is going on? Why is Asia doing so much better than Africa, with the understanding that we want to help Africa if we can?

Mr. HOLMES. When we make a decision to finance a feasibility study, you take a look at the project and you want to do a study on a project that you believe will eventually be financed. The fact of life is Asia, the Asian countries, are stronger than the African countries and they have access to lines of credit either internal or external that African countries don't have.

Nevertheless, we have been trying to operate in Africa. So, for that reason, some 25 of these 80 high risk feasibility studies in the investment window have been in African countries.

The window that concentrates on accessing strategic minerals and metals has been in African countries more than any other part of the world. We are now trying to go after World Bank financed projects and target on those. We have had some success.

You should note that we recently conducted one of our largest feasibility studies in Zimbabwe where we went after a bank project. We financed the feasibility study with $1 million. A Pennsylvania firm picked up a $4 million follow on contract and it was the first time in ages that the British have been shut out of Zimbabwe by an American firm.

The minerals window may be one of the areas where we are going to have some success. We just completed a technical mission to Senegal on titanium. DuPont picked up the results of the study on the titanium deposits in Senegal.

DuPont is 25 percent dependent on the Republic of South Africa for titanium slag. They wanted to diversify their sources of titanium and they bought up the mineral rights to that deposit in Senegal and they hope to make a $30 million investment. It takes a long time, but that is the gradual approach to dealing in that part of the world.

Senator KASTEN. What you are saying is that you are making progress and you are working toward doing more in Africa?

Mr. HOLMES. Yes. We are really trying.

Senator KASTEN. Thank you both for your testimony this morning. There may be additional questions that we will submit and ask that you get back to us with responses on the record.

OVERSEAS PRIVATE INVESTMENT CORPORATION

STATEMENT OF CRAIG A. NALEN, PRESIDENT AND CHIEF EXECUTIVE OFFICER, OVERSEAS PRIVATE INVESTMENT CORPORATION

INTRODUCTION OF WITNESSES

Senator KASTEN. Our next witness is Mr. Craig A. Nalen, who is the President and Chief Executive Officer of the Overseas Private Investment Corporation. We look forward to your testimony.

Mr. NALEN. Good morning, Senator. It is good to see you. This is Bob Draggon who is the Vice President for finance.

Mr. Chairman, if I may, I will submit for the record our statement?

Senator KASTEN. Without objection, your entire statement will be included in the record as if read.

Mr. NALEN. I will not intrude on your time with a repetition of what we have submitted here. I will, however, be pleased to answer any questions and perhaps make a very brief statement.

I think this is the first time we have appeared in front of this committee. We have appeared in front of some committees for the first time recently and have been asked to do a quick 60 second review of what OPIC is all about. I am not sure whether that would be appropriate here or not.

Senator KASTEN. Sure.

ACTIVITIES OF AGENCY

Mr. NALEN. Let me just say very briefly that we are a unique agency, different from the others, and I think the record would indicate that. The good news is that we don't cost the taxpayer anything. We do not require appropriations. We are a self-sustaining agency. That is, we make money; but, more about that in just a moment.

We were founded some 17 years ago, largely through the efforts of Senator Javits, to perform a basic function; that is, to encourage and enhance the investment by private U.S. countries into friendly third world countries.

We have two programs that do this. One is our insurance program, the other is our finance program. I will discuss those very briefly, but the idea was that investment in developing countries is extremely important towards their development. They certainly can't stand any more additional debt load.

Government-to-government concessional aid has never really been very effective, but perhaps the most effective means of bolstering these troubled economies is the injection of new capital; that is just what our programs are designed to do, thereby transferring management skills,

technology, creating new products, creating exports, and most of all creating the hope for a better quality of life.

At the same time, I will hasten to add, it is not a one-way street, particularly now in this critical time of American competitiveness. The opportunity for American companies to get footholds in these emerging markets is extremely important and one that has not been lost sight of by our competitors, Japan, Europe, and so forth. We are very much third, fourth, or fifth place in most of the developing world because of the aggressiveness of our competitors.

OPIC's programs try to keep American companies competitive and allow them to get footholds in these developing markets. It has been proven time and time again that from investment develops trade and increased trade is, of course, what it is all about these days.

INSURANCE PROGRAMS

Now, let me briefly describe the insurance program. It is political risk insurance. It is insurance we provide, for a fee, designed to relieve the investor of the concerns of what can happen in some of these unstable countries.

FINANCE PROGRAM

The finance program, which I think is what we are interested in today is a two-part program. One is our direct lending program, where we will lend money directly to a project sponsored by an American company. Our direct lending program is restricted entirely to small companies. Our investment guaranty is available to all businesses regardless of size.

Senator KASTEN. How do you define "small company"?

Mr. NALEN. Below the equivalent Fortune 1000, a loose knit description, but the best that we have been able to come up with. I might add that about two-thirds of our finance program, maybe not quite two thirds, go to the poorest of the poor countries, that is, the countries whose gross national product per capita is below $900 a year.

Geographically distributed, which is another sort of significant factor, about 40 percent of our projects are with the Caribbean and Latin American countries, 25 percent with African nations.

So our programs really are going to the right kind of clients, the smaller businesses. They are going certainly to the right parts of the world.

The reason we are here today—Let me just get back to the final thing where I said that we were self-sustaining. It might be confusing to somebody when you are talking about a Federal agency that makes money, but we do. We do not charge concessional rates, we charge market rates. We charge full rates for insurance, and full interest rates for our finance programs.

We, by statute, must be self-sustaining, Congress made us do that. This means that we operate quite autonomously and independently, not being able to be swayed by any part of the government to do a project or not do a project in a certain place. We try to balance our portfolio.

We have reserves of over $1 billion. Last year, we made a little over $100 million.

It is sort of an unusual story, but those are the facts.

LIMITS ON FINANCE PROGRAM

We are here today because this committee sets annual appropriation limits on our finance program, and our limits generally come in at what the administration recommends. Last year was an exception. OMB recommended that we have a $15 million limit on direct loans and a $150 million limit on loan guarantees. Last year Congress felt, based on the record, or for whatever reasons, that this should be increased to $23 million for the direct loan portfolio and $200 million for the loan guarantee program.

In summary, we don't require appropriations. We don't cost the taxpayer anything. We are helping the developing countries, and I think that we are helping United States companies at a very critical time to try to be competitive in the world marketplace.

I might add, in conclusion, that the limits that have been set on our finance program every year have been used to their fullest. In fact, the demand always exceeds the supply as it has in the last couple of years, and probably will this year, too.

(The prepared statement follows:)

PREPARED STATEMENT OF CRAIG A. NALEN

PRESIDENT & CHIEF EXECUTIVE OFFICER

OVERSEAS PRIVATE INVESTMENT CORPORATION

Mr. Chairman and Members of the Subcommittee:

It is a pleasure to have this opportunity to review the Finance Program of the Overseas Private Investment Corporation ("OPIC"). As this is the first time OPIC has formally testified before this Committee, let me take this opportunity to thank you for your past consideration and support.

Today, I will provide a general overview of OPIC and its activities before reviewing in some detail our Finance Program. Also, because U.S. trade policy is a major issue under current deliberation by the Congress, I will briefly discuss the relationship between overseas U.S. investment and trade, and the role of OPIC's finance and insurance services in promoting and facilitating U.S. trade.

General Overview

OPIC is a self-sustaining U.S. Government agency whose purpose is to encourage U.S. private investment in developing countries as a means for stimulating economic and social progress. OPIC assists U.S. investors in this effort through two principal programs: (1) the financing of investments through direct loans and loan guaranties; and (2) the insurance of investments by U.S. investors in private enterprises abroad.

In addition to its finance and insurance programs, OPIC

sponsors investment missions and operates a computer data system, both of which are designed to provide U.S. companies, particularly small businesses with little or no international experience, with information on specific investment opportunities and the business environment in developing countries.

OPIC commenced operations as an independent U.S. Government agency in January, 1971. As a self-sustaining agency, OPIC has received no public funds beyond its original start-up appropriations of $106 million which OPIC returned in full to the U.S Treasury three years ago. OPIC has recorded a net profit for every year of operation. The net profit for FY 1986 totalled $101.2 million and capital and reserves at September 30, 1986 exceeded $1 billion. OPIC's strong financial condition ensures its continuing ability to operate without requiring any Congressional appropriations.

Relationship Between U.S. Trade and Investment

Frequently, the close connection between overseas U.S. investment and U.S. trade is largely overlooked. Since U.S. investors naturally tend to procure U.S. capital equipment as well as to source on-going production inputs and spare parts from the United States, investment plays a key role in gaining access to new markets.

The need to expand U.S. export markets in developing countries is critical and urgent, given the unprecedented size of the U.S. trade deficit. At one time, the developing world absorbed as much as one-third of U.S. exports, a proportion that has declined to about one-quarter.

A recent study by the United Nations Industrial Development

Organization (UNIDO) demonstrates that industrialized countries have increased their industrial output and overall levels of employment as a result of increased trade with the industrializing Third World.[1] In particular, the UNIDO study estimated that the United States gained approximately 664,000 man-years of employment in one recent year alone (1983) as a result of its trade with these developing countries.

The introduction of American products and services to developing country markets by U.S. investors often spurs other U.S. exports to local consumers as they become familiar with American products, quality and standards. Foreign investment often allows U.S. firms to reach segments of the local market that cannot be served competitively from the United States.

OPIC's experience over the last five years supports these general observations. Through its finance and insurance activities, OPIC assisted some 676 projects over the FY 1982-86 period; these projects involved total U.S. investment of about $7.7 billion. An estimated 90 percent of that investment was immediately "recaptured" in the sense that some $6.8 billion of initial project procurements were U.S. exports. When follow-on procurement of U.S. production inputs over the first five years of project operations is added (an estimated $4.6 billion), the result is that U.S. exports total about 135 percent of the initial U.S. investment sum.

This strong positive connection between investment and trade has not been lost on our major competitors for these

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[1] Industry and Development: Global Report 1986, Vienna, 1986

Third World opportunities. While there are some significant assymmetries among the political risk insurance and finance programs operated by the United States, Europe and Japan, it is clear that OPIC's counterpart agencies are well organized to promote trade with developing countries through the encouragement of direct private investment in these countries.

Japan, which operates its program of project finance in developing countries under the auspices of its Export-Import Bank as well as its Overseas Economic Cooperation Fund, had an outstanding portfolio of direct loans, loan guaranties, and equity holdings of $7.1 billion at the end of 1985 compared to OPIC's current total direct loan and loan guaranty portfolio of $588.5 million. In 1985 alone, Japan issued $722 million in financing for projects involving direct Japanese private investment in developing countries, compared to $166 million for OPIC.

European competitors of the United States, including both the Federal Republic of Germany and the United Kingdom, also have direct loan and equity investment programs that are larger than OPIC's. Although Canada does not have a loan or loan guaranty program, its International Development Agency's Industrial Cooperation Program issued $40 million in grants in 1986 to Canadian companies for feasibility studies involving projects in developing countries. In all cases, our competitors justify these large programs in terms of the benefits they bring in increased exports to the developing countries as well as the host country development benefits of the projects themselves.

Finance Program Overview

OPIC's finance program provides medium to long-term financing for eligible U.S. businesses opening new business

ventures and expanding existing facilities in developing countries. It provides direct dollar loans in amounts ranging from $100,000 to $6 million. It also provides loan guaranties of up to $50 million per project as well as local currency loans.

In all cases, OPIC's participation takes the form of "project financing" based on the economic, technical, marketing and financial soundness of the project itself. Each project must be within the demonstrated competence of the proposed management, which must have a proven "track record" in an identical or similar line of business, as well as a continuing financial stake in the enterprise.

In providing project financing, OPIC makes every effort not to compete with commercial banks and other financial institutions, but seeks instead to complement private lending facilities. In addition, commercial banks frequently seek OPIC participation in project financing because they recognize that the presence of OPIC, as a U.S. Government corporation, can strengthen the prospects for project success. OPIC also works with the Export-Import Bank, U.S. Trade and Development Program, and the U.S. Agency for International Development ("A.I.D.") to provide a full range of services to U.S. firms exporting and investing overseas.

OPIC financing is particularly important for U.S. small business, which is often unable to obtain long-term funding for overseas projects on reasonable terms from private U.S. or developing country sources. In this connection, it is notable that approximately 70 percent of OPIC's annual project finance commitments since 1982 have been sponsored by, or have involved, significant participation by U.S. small business. In addition, the majority of OPIC's financings in dollar terms

during this five-year period have gone to projects located in the least developed countries -- those with per capita incomes of $896 or less in 1983 U.S. dollars.

Historical Performance - Finance Program

Since 1971, OPIC has made commitments for direct loans, loan guaranties and local currency loans in excess of $947 million to finance U.S.-sponsored projects in the developing world. Over half of these commitments were made during the last five years. During the FY 1982-86 period, OPIC made direct loans, loan guaranties and local currency loans of over $650 million in support of 119 projects in 44 developing countries.

Although OPIC receives no appropriated funds from Congress, this Committee is nonetheless responsible for setting the annual operating limits of our Finance Program. During FY 1986, the Finance Department fully utilized its financing authority of $13.6 million for direct loans and $136.4 million for loan guaranties. In addition, funding was committed for local currency loans totalling $2.9 million.

In FY 1987, Congress approved a ceiling of $2? million for direct loans and $200 million for loan guaranties. As of today, approximately three-fourth's of this year's authority has been utilized. The demand for our financial services remains strong and is expected to exceed the FY 1987 ceiling on both programs.

As noted above, as of September 30, 1986, the Finance Department portfolio, including authorized commitments not yet disbursed, amounted to $589.5 million. OPIC's Direct Investment Fund contributed $52 million to this total. In

dollar terms, the total Finance portfolio is distributed 25 percent in Africa, 40 percent in Latin America and the Caribbean, 23 percent in East Asia, and 12 percent in the Near East, South Asia, and Europe.

Direct Investment Fund (DIF) Program: Financing Small Business Investments

Since 1978, OPIC's Direct Loan Program has been reserved exclusively for small business. The demand for and utilization of the program has expanded steadily, consistently up to the limits of OPIC's authority. From FY 1982 through FY 1986, OPIC committed direct loans to 70 projects in 30 countries.

OPIC's Direct Loan Program has been especially effective in facilitating the participation of U.S. small business in the development of the Caribbean region and in support of the U.S. Caribbean Basin Initiative. Since 1982, over 65 percent of all OPIC direct loans have been made to projects in the Caribbean Basin.

An example of this type of project is the $400,000 financing package ($150,000 direct loan and $250,000 working capital line of credit) which OPIC provided to Fabrica Industrial de Alimentos de Honduras to expand a condiment packaging and processing plant in Honduras. This project will utilize $1.45 million of U.S. exports in the first five years of operation; developmental benefits will include increased employment for local farmers, import substitution and incremental foreign exchange earnings.

Another example of a recently financed project in the Caribbean region is the $1.6 million direct loan which OPIC provided to Corporacion Aeroporturia Del Este to expand and

improve a privately-owned, international airport in Punta Cana, Dominican Republic. The project has positive U.S. effects -- it will involve initial procurement of $540,000 in U.S. machinery and equipment. The project also has positive developmental effects for the Dominican Republic, providing employment for 200 workers during construction and 29 permanent employees thereafter. Upon completion, this project will stimulate tourism in an undeveloped eastern region of the Dominican Republic by increasing the accessibility of existing and planned hotel facilities.

A third example of our support for projects in the Caribbean is a $200,000 direct loan to Coiltronics, St. Kitts, Ltd. to expand a plant for manufacturing custom-designed inductive and electro-magnetic components. This project, which involves initial U.S. procurement of $225,000, is expected to generate over $4.6 million in foreign exchange earnings for St. Kitts in the first five years of operation. With the potential to create over 320 jobs, this project will provide for the transfer of new electronics technology and skills, an important diversification for St. Kitts' agrarian-based economy.

Local Currency Loans

On behalf of the A.I.D., OPIC administers the Cooley Loan Program, which lends excess local currency obtained by the U.S. Government through P.L. 480 sales of agricultural commodities to appropriate projects in developing countries. Since FY 1982, OPIC has made eight Cooley Loans, all in Pakistan, for a total amount of local currency equivalent to U.S. $15.7 million. Five of the projects have involved the manufacture of basic pharmaceutical products. Funding for this program is contingent on the availability of local currency under relevant A.I.D. programs in Pakistan.

In FY 1986, OPIC was given the additional responsibility of administering loans on a broader geographical basis under Section 108 of P.L. 480. OPIC expects to fund its first local currency loans under this program in Jamaica and/or Costa Rica in FY 1987.

Loan Guaranty Program

OPIC's Loan Guaranty Program provides U.S. financial institutions with guaranties -- backed by the full faith and credit of the United States -- for loans made to eligible U.S. investors for projects in developing countries. These guaranties protect against commercial as well as political risks.

An OPIC-guaranteed loan can provide investors with a significant portion of medium to long-term borrowing for ventures in countries where conventional financial institutions are reluctant to make commitments. Thus, OPIC's Loan Guaranty Program supplements the lending and investing facilities of commercial banks, as well as local, regional and international development banks. Such guaranties also play an important catalytic role in attracting funds from a variety of sources (including multilateral institutions) to a number of highly developmental, capital-intensive projects in poorer developing countries.

One example of such a loan guaranty is OPIC's recent commitment of $20 million to the Africa Growth Fund. This Fund is a major new initiative developed by OPIC to mobilize equity capital by establishing an investment company to encourage development of U.S.-sponsored projects in sub-Saharan Africa. Investments from the Africa Growth Fund will be in a broad range of industries and countries, supporting U.S. foreign policy objectives.

Another example is a $5.9 million OPIC loan guaranty to the Liberian Agricultural Company. This loan will be used to expand the company's existing rubber plantation and processing plant. The Liberian economy will benefit from the creation of 600 new jobs. In addition, the plant expansion will permit the facility to process the output of nearby smallholders.

As of September 30, 1986, committed and outstanding OPIC loan guaranties totalled $536.5 million. Of this amount, 27 percent, or $144 million, represents funding for projects in sub-Saharan Africa.

Environmental Review Procedures

OPIC has a long-standing policy of trying to assure that the projects it supports are environmentally sound and that such projects utilize natural resources in a sustainable manner. The host country environmental impact of every potential finance and insurance project is assessed at the time of application. Following this assessment, project modifications are made as necessary. A project may be rejected on environmental grounds alone if it does not meet the criteria outlined by Congress in our legislation. Furthermore, in accordance with our legislation, we have a regular system of notifying host government environmental officials, in advance of approval, of our concerns regarding the potential environmental sensitivity of the projects for which we are considering providing assistance.

Examples of OPIC Support of U.S. Exports

OPIC supports developmental projects which have positive trade benefits for the United States. OPIC's $150 million in FY 1986 financing alone (not counting insurance) will generate

an estimated $273 million in initial U.S. procurement and $171 million in additional production inputs over the next five years. That translates into some 2,500 man-years of employment for U.S. workers.

A recent example demonstrating the linkage between direct investment and trade involves a project to which OPIC extended an $11 million loan guaranty to finance a flour mill in Cameroon. The U.S. parent company projects annual direct sales of over 90,000 metric tons of U.S. wheat, or roughly $96 million, to the project over the life of the 8-year loan, thus tapping into a market currently dominated by the French.

The Finance Department has developed a Small Contractors' Guaranty Program to help small U.S. companies compete more effectively in Third World markets. Small U.S. companies often experience difficulty obtaining credit for working capital and to support bid and performance bonds when pursuing international contracts. In addition, they often compete against foreign bidders receiving government assistance. OPIC's program helps meet the competition by guaranteeing U.S. financial institutions for up to 75 percent of the amount of letters of credit posted to cover small U.S. contractors' performance or advance payment guaranties.

An example of how OPIC's Small Contractors' Guaranty Program can make U.S. small businesses competitive in the international marketplace is our guaranty of $2.6 million to Evergreen International Aviation. With our guaranty, this small West Coast company was able to bid successfully and win a contract which involved aerial spraying for control of "river blindness" in 11 West African countries, beating out a Canadian firm receiving assistance from the Canadian government.

OPIC has also designed a Distributorship Program to help U.S. equipment manufacturers finance overseas dealerships of U.S. heavy equipment. Through loans or loan guaranties, this program effectively and directly stimulates U.S. exports. Utilizing this program, OPIC has made available a credit facility to local distributors for the expansion of existing Mack truck and Caterpillar facilities in Central America.

Protecting U.S. Employment and the U.S. Economy

Pursuant to Congressional directives, OPIC screens each proposed investment--and selectively monitors these investments after they are made--to ensure that they contribute positively to the development of the host country and that they will not have a significant adverse effect on the U.S. economy or U.S. employment.

OPIC's economists analyze the probable impact of every proposed project on the U.S. investor, the industry sector involved and related business sectors. Such factors as the level of U.S. employment, the sensitivity of the relevant sector to imports, the competitiveness of U.S. exports in foreign markets, the imposition of trade-related performance requirements by the host government and other relevant factors are considered.

Consistent with Congressional intent, OPIC refuses to assist those projects that are clearly "runaway" plants or any other investment that might have a significant adverse effect on U.S. employment. OPIC formally rejected 17 projects on this basis in FY 1986 alone. This is the largest number of projects rejected in any single fiscal year and the highest proportion of projects rejected by OPIC since FY 1978. Since 1974, OPIC has formally declined to issue insurance or financing for 129

projects on the basis of adverse U.S. effects. Many other projects have been informally discouraged in the early stages of the applications process based on preliminary indications that the project would be likely to have an adverse effect on U.S. employment or the U.S. economy.

Conclusion

Our Finance Program, through direct loans and loan guaranties, thus helps OPIC exercise both its development and trade mandates.

OPIC's Direct Loan Program has been particularly effective in furthering the Caribbean Basin Initiative and in providing significant support to projects involving U.S. small business. Our Loan Guaranty Program complements private lending facilities and plays an important role in attracting investments and mobilizing financing for highly developmental, capital-intensive projects in the least developed countries, and, most notably, those in Africa.

Furthermore, projects supported by our loan guaranties and direct loans generate substantial U.S. exports and thus create positive U.S. employment effects. By supporting developmental projects with positive U.S. trade benefits, we broaden U.S. participation in world trade and strengthen our country's competitive position in the world's fastest growing markets--those in the Third World.

Although our finance activities are relatively small compared to other U.S. Government programs and many of our

counterparts in other OECD countries [2], we believe that as a self-sustaining agency, we are near the top in cost/benefit terms. The cost to the U.S. Treasury is minimal and the benefit to both the host country and the U.S. economy is clear.

I would be pleased to respond to any questions which you and the Committee may have.

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[2] A Comparative Study of the Official Programs of Selected OECD Countries that Provide Financing to Private Investors for Projects in Developing Countries, Ghadar Associates, 1985.

OPIC

DEVELOPMENT EFFECTS/FINANCE PROGRAM RESULTS

FY 1981 - 1986

Total Project Investments	$ 5,109,505,742
U.S. Effects	
Total Direct U.S. Exports (5 -years & initial procurement)	$ 2,748,734,378
U. S. Employment Effects (5 years)	26,360 man-years
Developmental Effects	
Annual Exports Generated	$ 2,172,667,909
Annual Imports Replaced	$ 432,885,388
Net Foreign Exchange Impact	$ 1,116,415,480
Total Local Labor Impact	29,118 persons

SUPPORT FOR ADMINISTRATION PROGRAM

Senator KASTEN. We are back, as I understand it, with the administration asking $15 million instead of $23 million, which you were able to utilize last year, and instead of $200 million, which you were able to use on the guarantee side, back at $150 million, which is a 34 percent cut and a 25 percent cut respectively. These are OMB's recommendations; is that right?

Mr. NALEN. It is the administration's position, and we support it.

Senator KASTEN. What impact would these cuts have on OPIC's programs?

I understood you to say that you have been able to utilize the full extent of the dollars and guarantees that have been appropriated in the past.

Mr. NALEN. The impact would be that we would have to cut back on our program by some 40 percent. This would mean fewer companies would be encouraged to invest in the third world, and fewer U.S. companies would be competing in the world marketplace.

Senator KASTEN. Let me talk specifically about Africa. You pointed out that 40 percent was in the Caribbean, but it is our understanding that you are planning to launch an Africa growth fund program with specific emphasis, maybe even emphasis on the Subsaharan Africa.

Mr. NALEN. Yes.

Senator KASTEN. Could you talk to us a little bit about how this African growth fund would work, and what is it that you are trying to do there that you have been unable to do before?

Mr. NALEN. We are trying to do projects in Africa.

DEBT AND EQUITY QUESTION

Senator KASTEN. Let me just go further. There is a debt and equity question here also, so if you could cover that in your response.

Mr. NALEN. Africa has been a tough place to try to get American companies to do business. We have been extraordinarily lucky there, having flour mills in Cameroon, and hotels on the Ivory Coast, and fishing operations in Ghana. But if you really dig deep, each one is a difficult one to do.

It was our feeling that if we could help put together a fund of capital to be available for U.S. companies to invest in Africa, it would be the first of its kind. It would be underwritten partially by OPIC, a $30 million fund, $20 million would be guaranteed through our loan guarantee program by OPIC, and the other $10 million would be contributed by U.S. companies.

We felt that there are a number of U.S. companies who, for whatever reason, be it political, moral, or just plain good business sense, feel that there ought to be a greater American presence in Africa. They would contribute the remaining $10 million, and they would then help find U.S. companies uniquely suited to undertake projects in Africa.

Many of these are large companies who would contribute to this $10 million fund; but they would have supplier companies that are doing

peripheral business in Africa, and perhaps they could start establishing bases over there.

The concept is excellent. It is still too soon to tell you how it is going to work out. We have First Boston who is helping us raise the equity. The Equator Bank is going to administer it.

It is a marvellous example of the public and private sector forming a close link here, trying to penetrate the major challenge of getting some businesses going.

Senator KASTEN. Is this the first time that OPIC is going to provide equity as well as debt for projects?

Mr. NALEN. Yes, it is.

We have a related program io the Philippines, which is the First Philippine Capital Fund, through our insurance program.

This is rather complicated, but let me try to explain. It is designed to encourage debt/equity swaps in the Philippines, and encourage privatization of parastatal entities over there.

AFRICAN GROWTH FUND

Senator KASTEN. In the African Growth Fund, you are going to be providing both equity and debt?

Mr. NALEN. We are guaranteeing $20 million of the $30 million pot of capital, the rest of it is going to be contributions of equity coming in from the private sector.

Senator KASTEN. First Boston is raising it?

Mr. DRAGON. Yes, $10 million to match the OPIC $20 million. That fund will then invest in up to 30 projects using the $30 million.

If additional debt is needed in a particular project, OPIC could also step in through its finance program and provide additional financing.

We anticipate the fund to go into operation sometime in the fourth quarter of this year, if we are successful in raising the equity, and it will be implemented in the following two years.

Senator KASTEN. There may be a couple of additional questions that we will submit to you for the record.

I just want to say, as the Ranking Minority Member on this subcommittee, we are going to look carefully at those OMB numbers. I appreciate and enthusiastically support what you have been able to do, and we want to help you and work with you in every way that we can.

We thank you very much for your testimony.

Mr. NALEN. Thank you for listening, we appreciate it.

SUBMITTED QUESTIONS

[The following questions were not asked at the hearing, but were submitted to the Agencies for response subsequent to the hearing:]

Questions Submitted by Senator Inouye to Mr. Bohn

SENATOR INOUYE: A recent issue of "Inside U.S. Trade", which discussed the negotiations with the Europeans on "mixed credits", contained the following statement: "Exim hopes France and Italy will back away from using mixed credits when they realize the U.S. has a lot more money for this kind of financing than they do." As you know, the amount of funds available under the foreign affairs function is steadily decreasing. In light of this trend, does the U.S. have a lot more money for mixed credits than do the Europeans?

MR. BOHN: The U.S. has negotiated an agreement with the OECD countries that should result in a decrease in the availability of resources for tied aid credit from all sources. The reason for the probable decline is that each tied aid credit transaction will now be considerably more expensive to support since the minimum allowable level of concessionality was increased significantly (from 25 percent to 35 percent).

Hence, it is too early in the agreement's tenure to determine if the increase in the minimum concessionality level will limit the availability of tied aid credit resources. However, the fact that more funds will have to be utilized to support the same level of tied aid transactions indicates that the available resources for tied aid credits is diminished.

SENATOR INOUYE: The member nations of the OECD have reached agreement on the use of mixed credits which attempts to establish standards for deciding which nations should be eligible and at what levels mixed credits should be available.

Is the recent OECD agreement on mixed credits far reaching enough that the use of mixed credits by major exporters will be eliminated? If not, what posture should we take to insure that the U.S. exporters remain competitive?

MR. BOHN: Tied aid credits will not likely be eliminated as a result of the new tied aid credit agreement; however, the incidence of tied aid credits should decline since the costs to the donor countries in providing tied aid credits are significantly increased.

Any departure by an OECD member country from the rules established by the new tied aid credit agreement are subject to retaliatory measures from the U.S. Eximbank closely monitors the financing terms provided by OECD export credit agencies. The Bank's policy is to at least match nonconforming financing offers, or in some cases provide even more generous financing terms indicating the full commitment of the U.S. Government to discourage extraordinary subsidized financing. Hence, in most instances, U.S. exporters will have access to fairly competitive financing.

SENATOR INOUYE: Will the mixed credit War Chest that the Administration has requested be more than a negotiating tool?

MR. BOHN: The War Chest is intended primarily to be used to police the OECD tied aid credit agreement. Any nonconforming financing terms provided by an OECD country's government will prompt an investigation to determine if the War Chest is an appropriate mechanism to utilize in responding to the foreign financing offer.

SENATOR INOUYE: Do you have adequate legal authority to offer mixed credits?

MR. BOHN: Yes, Eximbank has adequate legal authority to offer mixed credits.

SENATOR INOUYE: Do you have sufficient funds for mixed credits so that U.S. exporters will be able to successfully compete?

MR. BOHN: The effect of the OECD tied aid credit agreement is difficult to quantify at this time since the new rules have only recently been implemented. However, the successful negotiation of a tied aid credit agreement in all probability will reduce the level of resources required to combat illegal tied aid credit offers. Therefore, the resources available to the Bank appear to be adequate to meet the U.S. Government's objective in the tied aid credit area.

SENATOR INOUYE: Does the Administration have the will to use mixed credits?

MR. BOHN: The Administration is fully committed to establish and maintain discipline in the OECD agreement on tied aid credits. It is in that context that mixed credits will be utilized by Eximbank to retaliate against violations of the agreement.

SENATOR INOUYE: In the 1987 authorization for the Eximbank, the Congress directed that the Bank modify the guarantee program so that the guarantees offered by the Bank are fully transferable. The detailed conditions under which these guarantees would be transferred have been under discussion for several months. It is my understanding that the National Advisory Council, which was scheduled to meet last week, is responsible for developing Administration policy in this area.

a) Did the Council reach a consensus on conditions for transferring the guarantees?
b) In your judgment, are these conditions proposed by OMB and the Treasury Department realistic?
c) Will they permit the easy transferability of these guarantees?

MR. BOHN: Free transferability of obligations guaranteed by Eximbank is mandated by the Export-Import Bank Act Amendments of 1986. Eximbank has developed procedures and documentation that will enable such transferability to take place with a minimum of administrative inconvenience. The National Advisory Council, including OMB and the Treasury Department, provided Eximbank with advice on the rate of interest Eximbank should guarantee. In arriving at this rate, Eximbank balanced the need to set rates at a level which will realistically permit obligations guaranteed by Eximbank to be sold in the private capital markets with the desirability of keeping potential costs to the U.S. taxpayer as low as possible. For these reasons, Eximbank has set the current guaranteed interest rate at the lesser of (a) the rate on the obligation being guaranteed by Eximbank minus fifty basis points or (b) the Treasury rate on obligations of similar maturity plus fifty basis points, the LIBOR (London Interbank Offer Rate) rate on obligations of similar maturity minus twenty-five basis points or the Prime rate on obligations of similar maturity minus two hundred basis points. These rates should have no adverse effect on the transferability of Eximbank guarantees.

Questions Submitted by Senator Inouye to Mr. Levy

TRADE CREDIT INSURANCE PROGRAM (TCIP)

SENATOR INOUYE: In recent years this committee has funded a number of private sector initiatives in A.I.D. In addition to the program which you oversee, the committee has funded the establishment of the private sector revolving fund.

One of the private sector revolving fund's principal activities is to provide funds to banks and other financial institutions in developing countries.

You supply credit insurance to similar institutions.

How do these two programs differ?

Are the TCIP program and the private sector revolving fund coordinated?

MR. LEVY: The TCIP and the Private Sector Revolving Fund both respond to private sector credit needs in developing countries. However, they are really quite different programs, directed towards different problems.

The Revolving Fund enables A.I.D. to invest directly in the private sector in developing countries, so as to foster economic growth and development. This results in job creation, foreign exchange generation and technology transfer. The Revolving Fund operates worldwide and while in some cases, as a result of its loans, borrowers increase their imports this is not an exclusive focus of the program. The major charge of the Revolving Fund is to promote the development of the private sectors in developing countries with special emphasis on strengthening local private financial institutions and diversifying the credit sectors.

The TCIP responds to a perceived lack of foreign exchange to fund necessary imports for the private sector in Central America. Under the TCIP, A.I.D. does not lend government funds; rather guarantees are issued to U.S. banks which, in turn, make available short-term lines of credit to local banks to finance imports from the United States.

SENATOR INOUYE: According to documents you have supplied the Committee, during calendar year 1986 the TCIP program guaranteed $109 million in trade transactions in the four Central American countries in which the program is operating.

What level of incremental trade resulted from these guarantees?

MR. LEVY: Unfortunately, neither we nor the Export-Import Bank are able to answer this question completely. While the figures indicate that more than $165 million in U.S. exports were financed under the Program during 1986, we do not know how many of these transactions would have taken place had the program not been in operation.

The program should also facilitate exports from the participating countries. Many of the items imported from the United States under the program are then utilized in the manufacture of goods for export. We do not have data, however, which can relate specific exports from Central America to transactions under the program.

Early in fiscal year 1988, we expect to undertake an evaluation of the TCIP. At that time we will see if, on a sampling basis, we can obtain data that would permit us to respond more completely to this question.

Questions Submitted by Senator Inouye to Mr. Holmes

DEVELOPMENT AGENDA OF THE TRADE AND DEVELOPMENT PROGRAM

SENATOR INOUYE: I want to complement you for delivering your statement to the Committee well ahead of time. It is an excellent statement that makes a strong case for the success of the TDP programs. American exporters have clearly benefitted from the effectiveness of your efforts.

Your statement, however, makes little reference to the development impact of your activities.

Is the development agenda of the program receiving the attention it deserves? What are you doing in this regard?

MR. HOLMES: I do believe that the development agenda of the Trade and Development Program (TDP) is receiving the attention it deserves. We are attending to the development agenda in the following fashion.

In all the countries in which we operate, we concentrate first on financing feasibility studies for those projects which are contained in a country's national development plan. In this regard, we also attempt to give high priority to projects which either are being financed by or stand a strong chance of being financed by, the major international development banks,particularly the World Bank, the African Development Bank, the Inter-American Development Bank, and the Asian Development Bank. Additionally, we have targetted on certain sectors which have very high developmental priority to Third World nations. These sectors include, hazardous and solid waste management and disposal, training, telecommunications, and power generation. We have concentrated on these sectors not only because of their developmental importance to a country, but also because these sectors represent major export markets for U.S. firms.

Finally, we see a major developmental impact of our program in the form of overall technology transfer. When TDP finances the planning of a major project, such as a power station, a significant element of the feasibility study is identifying appropriate technologies and setting forth a plan in which these technologies can be transferred to the developing country. All too often, developing countries have embarked on projects with inadequate planning which has cost them significant economic hardships downstream. By helping developing countries undertake first-rate planning of a major project, we believe we are in turn making a significant contribution to the overall development of the country.

QUESTIONS SUBMITTED BY SENATOR INOUYE TO MR. NALEN

SENATOR INOUYE: I understand that in 1988, OPIC is planning to launch an innovative "Africa Growth Fund." There is a world-wide consensus that more must be done in sub-Saharan Africa.

Would you explain how the "Africa Growth Fund" will be innovative? I understand that this is the first time that OPIC will provide equity as well as debt for projects.

MR. NALEN: OPIC's finance program has committed $250 million to development in sub-Saharan Africa, which is a substantial amount in view of the comparatively few American companies that have invested in the region. Yet, we are seeking to accomplish much more there.

During the past year, we have taken a careful look at how OPIC could further stimulate investment interest in sub-Saharan Africa. We have sought ways, including innovative ones that we had not considered before, to support the changes underway in the region by using the authorities already granted to us by the Congress. One result is the Africa Growth Fund.

The Africa Growth Fund is an innovative investment vehicle designed to raise capital for creating, expanding and/or rehabilitating productive business enterprises in sub-Saharan Africa, thereby generating vital new economic activity, private-sector growth and employment opportunities throughout the targeted region.

The Fund is designed to be a privately-owned limited partnership having investment capital of $30 million. Equity capital will total $10 million in the form of limited partnership interests offered to substantial American corporate investors. Debt capital of $20 million will be created through OPIC-guaranteed promissory notes issued to qualifying American financial institutions. The fund is intended to have a 15-year term.

The Africa Growth Fund seeks to achieve long-term appreciation and a current return on its capital primarily by investing in equity and equity-related securities of companies in sub-Saharan Africa. Companies in which investments are made will be chosen by OPIC in consultation with other participants on the basis of their sound financial condition and/or attractive growth potential, and their favorable host country developmental and U.S. economic benefits. The Fund intends to purchase securities of both new and established companies planning to expand or modernize, requiring significant capitalizations to increase their competitiveness, or intending to implement privatization from a previously state-owned structure.

The 40 sub-Saharan countries targeted by the Africa Growth Fund offer a broad range of potential investment opportunities. With our program, we hope to demonstrate that U.S. private investment is possible in Africa.

SENATOR INOUYE: One of OPIC's principal activities is providing loans directly to U.S. small businesses to invest in new business ventures overseas.

In the United States, small business are a major creator of new jobs. Do OPIC's loans mean fewer jobs for American workers?

MR. NALEN: Section 231(e)(2) of the Foreign Assistance Act obliges OPIC to undertake to increase the proportion of its projects sponsored by or significantly involving United States small business to at least thirty percent of all projects.

In enacting this provision, Congress sought to insure that smaller American businesses would be given priority consideration in the operation of OPIC's programs so that they can compete successfully in the world economy. Congress was also mindful that OPIC is primarily a development agency, that generation of employment in developing countries is a critical need, and that smaller businesses tend to generate a substantial number of jobs both in the U.S. and abroad. In FY 1986 forty percent of OPIC-supported projects were undertaken by small and medium-sized U.S. businesses.

There is no causal relationship between jobs created in developing countries and the loss of employment in the United States. Indeed, OPIC's experience is to the contrary. In FY 1986 the 56 OPIC-supported projects sponsored by small and medium U.S. firms are expected to result in the creation of about 6,500 jobs in the developing nations. These same projects will create an estimated 1,800 man-years of employment in the U.S. as a result of initial and on-going operational procurement. Since OPIC will not support any project involving a runaway plant, none of these projects resulted in the closure of small businesses in the United States.

It is, in OPIC's judgment, critically necessary that American small and medium-sized business continue to have access to OPIC's services. Investment abroad enables these firms to compete more successfully in the world economy and for many firms, overseas investment is their only hope for survival.

SENATOR INOUYE: The 1987 Continuing Resolution contained two provisions designed to prevent AID from subsidizing exports from developing countries which could injure U.S. businesses.

The Bumpers Amendment restricts AID funding of projects which would compete with U.S. agricultural commodities.

The Lautenberg Amendment forbids AID to assist directly "in the establishment of facilities for the manufacture for export to the U.S. of...import sensitive articles..."

Do similar restrictions apply to OPIC?

How does OPIC deal with the concerns raised by this Amendment?

MR. NALEN: Three sections of OPIC's statute specifically address the concerns raised by your questions. Section 231(k) of the Foreign Assistance Act of 1961, as amended, provides that OPIC cannot support a project if it is determined that:

> "such investment is likely to cause [an] investor...significantly to reduce the number of his employees in the United States because he is replacing his United States production with production from such investment which involves substantially the same product for substantially the same market as his United States production;"

Section 231(l) further forbids the Corporation from supporting any project "if the Corporation determines that such investment is likely to cause a significant reduction in the number of employees in the United States."

Finally, with respect to exports, the Corporation is enjoined in Section 231(m) from assisting any project "subject to performance requirements which would reduce substantially the positive trade benefits likely to accrue to the United States from the investment." Thus, if a developing country's laws or regulations compel an investor to export agricultural items to the U.S. or elsewhere which would reduce substantially U.S. trade benefits, OPIC cannot assist that project. In addition, OPIC is directed by Section 231(h) "to further to the greatest degree possible, in a manner consistent with its goals, the balance-of-payments and employment objectives of the United States."

Pursuant to these provisions of law and the Corporation's own policies directed at protecting the U.S. economy and U.S. jobs, OPIC's Board of Directors has promulgated detailed guidelines covering projects producing agricultural commodities in world surplus and projects involving textiles. The Board has also issued explicit guidance on how proposed projects are to be analyzed to ensure that all the above-cited statutory requirements are met.

OPIC economists review <u>each and every</u> prospective OPIC project to ensure that it meets

the criteria established by Congress and its Board. To the best of our knowledge, the Corporation has never supported a project which has had a significant adverse impact on American jobs or the U.S. economy. It should be noted that, pursuant to Section 240A(c)(1), a study by a major independent accounting firm is now underway and will be completed by December, 1987, which reviews about 150 OPIC-assisted projects to verify that OPIC projects have not adversely affected the U.S. economy.

SUBCOMMITTEE RECESS

Senator KASTEN. The subcommittee will now stand adjourned until Thursday, July 30, when the committee will receive the testimony of public witnesses.

[Whereupon, at 10:35 a.m., Tuesday, July 28, the subcommittee was recessed, to reconvene at 9:00 a.m., Thursday, July 30, 1987.]

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